172947

Progress Energy

March 1, 2005

RECEIVED
2005 MAR -2 PM 12:35
SC PUBLIC SERVICE COMMISSION

Mr. George N. Dorn, Jr.
South Carolina Public Service Commission
Interim Executive Director
ATTN: Docketing Department
P.O. Drawer 11649
Columbia, SC 29211

RE: Progress Energy Carolinas, Inc.'s Application for Authority to Issue Securities Pursuant to Revolving Credit Agreement

Dear Mr. Dorn:

Enclosed for filing are the original and twelve (12) copies of Progress Energy Carolinas, Inc.'s Application for Authority to Issue Securities Pursuant to Revolving Credit Agreement. Please date stamp two of the enclosed copies and return them to the bearer of this letter.

Sincerely,

Len S. Anthony
Deputy General Counsel-Regulatory Affairs

LSA:bba
c: Dan F. Arnett, Office of Regulatory Staff
222243

Progress Energy Service Company, LLC
P.O. Box 1551
Raleigh, NC 27602

172947

ACCEPTED
Legal 2013 3-2-05

STATE OF SOUTH CAROLINA
BEFORE THE PUBLIC SERVICE COMMISSION OF SOUTH CAROLINA
DOCKET NO. 2005-39-E

In the Matter of	)	APPLICATION FOR AUTHORITY TO
	)	ISSUE SECURITIES PURSUANT TO
Progress Energy Carolinas, Inc.	)	REVOLVING CREDIT AGREEMENT

RECEIVED 2005 MAR -1 PM 12:35 SC PUBLIC SERVICE COMMISSION

Pursuant to the S.C. Code Ann. Section 58-27-1710 (as amended 1976) and Public Service Commission of South Carolina Rule 103-834, Progress Energy Carolinas, Inc. (the "Company") respectfully applies to the Commission and represents as follows:

1. The Company's correct name and post office address are Progress Energy Carolinas, Inc., Post Office Box 1551, Raleigh, North Carolina 27602. The names and post office address of its attorneys are Len S. Anthony and Patricia Kornegay-Timmons, Post Office Box 1551, Raleigh, North Carolina 27602. The Company is a corporation organized and existing under the laws of the State of North Carolina, and authorized to do business in South Carolina. Its principal office is located at 410 S. Wilmington Street, Raleigh, North Carolina, 27601. The Company is primarily engaged in the business of generating, transmitting, delivering and furnishing electricity to the public for compensation.

2. The Company's capital stock outstanding at September 30, 2004 consisted of Common Stock with a stated value of $1,897,000,000 and Preferred Stock with a stated value of $59,000,000. As of September 30, 2004, the retained earnings of the Company were $1,338,000,000.

The Company's existing long-term debt at September 30, 2004, amounted to principal amounts of $2,268,725,000 in First Mortgage Bonds and $800,000,000 in other long-term debt. The First Mortgage Bonds were issued under and pursuant to an Indenture of Trust dated as of May 1, 1940, duly executed by the Company to The Bank of New York (formerly Irving Trust Company), as Corporate Trustee, and Frederick G. Herbst, as Individual Trustee, succeeded by W. T. Cunningham, who presently is acting as Individual Trustee, as supplemented by seventy-two Supplemental Indentures.

3. The Company currently maintains two revolving credit agreements totaling

$450,000,000 – one is a $165,000,000 364-day agreement, the other a $285,000,000 3-year agreement. The revolving credit agreements provide back-up liquidity for the Company's lower-cost commercial paper program. The Company proposes to negotiate and enter into a new 5-1/4-Year revolving credit agreement in order to secure long-term liquidity in the current accommodative bank market, and to meet the Company's continuing short-term capital needs arising in connection with the provision of electricity and related services to the Company's customers. The proposed revolving credit agreement will replace the Company's two existing revolving credit agreements. This Application relates to the proposed new 5-1/4-Year Revolving Credit Agreement (the "5-1/4-Year RCA") with Wachovia Bank, N.A. ("Wachovia") and the Royal Bank of Scotland plc ("RBS") as agents for certain Lender banks. The terms and conditions of the 5-1/4-Year RCA are set forth in the Summary of Terms and Conditions, substantially in the form attached hereto as Exhibit A. The amount of the 5-1/4-Year RCA is up to $500,000,000. The 5-1/4-Year RCA will have an initial term of five-1/4 years. Under the 5-1/4-Year RCA, the Company will have the option of two different interest rates per annum on any borrowings, as set forth on page 2 of Exhibit A and the Pricing Grid attached thereto.

4. The Company estimates that it will incur expenses of approximately $1,000,000 in connection with the negotiation and execution of the 5-1/4-Year RCA. Additionally, the Company will be charged a facility fee which can range from 8 basis points to 25 basis points based upon the ratings of the Company's long-term, unsecured, senior, non-credit enhanced debt by Standard & Poor's or Moody's in accordance with Exhibit A and the Pricing Grid attached thereto.

5. The Company requests that the Commission authorize the Company to make minor modifications and amendments to the 5-1/4-Year RCA as the Company and the participating Lender banks deem necessary from time to time, including extending the term of the 5-1/4-Year RCA for an additional two years; provided, however, that in no event would the Company amend the 5-1/4-Year RCA to increase the amount of the total commitment above $500,000,000 without the prior approval of the Commission.

6. Information required for compliance with Order 91-72 in Docket No. 91-032-E is provided in the Attachment to this Application.

7. The purposes for which the proposed transaction is to be affected, as described

above:

(i) Are for a lawful object within the corporate purposes of the Company;

(ii) Are compatible with the public interest;

(iii) Are necessary and appropriate for and consistent with the proper performance by the Company of its service to the public as a utility;

(iv) Will not impair the Company's ability to perform its public service; and

(v) Are reasonably necessary and appropriate to provide adequate funds for such corporate purposes.

WHEREFORE, the Company prays that this Commission issue an Order:

A. Authorizing, empowering and permitting the Company to enter into the 5-1/4-Year RCA as described in this Application, to issue securities in the form of commercial paper and other short-term financing pursuant to the 5-1/4-Year RCA at such times as the Company desires to borrow funds pursuant to the 5-1/4-Year RCA, and to execute and carry out such instruments, documents and agreements as shall be necessary or appropriate in order to effectuate the transactions contemplated by the 5-1/4-Year RCA;

B. Approving the terms and conditions of the 5-1/4-Year RCA in substantially the form described in this Application; and

C. Authorizing, empowering and permitting the Company to make minor modifications and amendments to the 5-1/4-Year RCA as the Company and the participating Lender banks deem necessary from time to time, including extending the term of the 5-1/4-Year RCA for an additional two years; provided, however, that in no event shall the Company amend the 5-1/4-Year RCA to increase the amount of the total commitment above $500,000,000 without the prior approval of this Commission.

This _____ day of March, 2005.

PROGRESS ENERGY CAROLINAS, INC.

By: ______________________________
Thomas R. Sullivan
Treasurer

____
Len S. Anthony
Deputy General Counsel
Patricia Kornegay-Timmons
Associate General Counsel
Progress Energy Service Company
P. O. Box 1551
Raleigh, North Carolina 27602
(919) 546-6367

221625

STATE OF NORTH CAROLINA

COUNTY OF WAKE

Before me, Brenda B. Addison, a Notary Public in and for the County and State aforesaid, this 1st day of March, 2005, personally appeared Thomas R. Sullivan, to me known to be the person whose name is signed to the foregoing Application, and, after first being duly sworn, made oath and said that he is the Treasurer of Progress Energy Carolinas, Inc., that he has read the foregoing application and knows the contents thereof and that the same is true and correct to the best of his knowledge, information and belief.

Brenda B. Addison
Notary Public

My Commission Expires: 5/19/2009

BRENDA B. ADDISON NOTARY PUBLIC ORANGE COUNTY, N.C.

221625

ATTACHMENT TO APPLICATION FOR AUTHORITY TO ISSUE SECURITIES PURSUANT TO REVOLVING CREDIT AGREEMENT FILED IN PUBLIC SERVICE COMMISSION OF SOUTH CAROLINA DOCKET NO. ______

In compliance with Order 91-72 issued in Docket No. 91-032-E, the Company hereby provides the following information in connection with the above-referenced Application:

a. The Company's Consolidated Financial Statements as of December 31, 2003, and Consolidated Interim Financial Statements as of September 30, 2004 are attached as Exhibit B and Exhibit C, respectively. The Company's Pro Forma Consolidated Balance Sheet and Pro Forma Consolidated Income Statement showing the impact of the proposed revolving credit facility on the Company are attached as Exhibit D. The pro forma data indicates that the revolving credit agreement will not materially impact the Company's Consolidated Financial Statements.

b. The 5-1/4-Year RCA is an essential element of the Company's commercial paper borrowing program as it provides back-up liquidity for this program in the event of a disruption in the commercial paper market. The Company's rating agencies require such backup facilities in order to maintain the ratings on the Company short-term obligations.

c. If the authority to issue securities pursuant to the 5-1/4-Year RCA is delayed or not approved, the Company's access to low-cost commercial paper will be impaired. The 5-1/4-Year RCA is intended to provide back-up liquidity for the Company's issuances of commercial paper. Such low-cost debt generally is only available to debtors in the financial markets if they provide creditors with some sort of back-up liquidity for the debt. The Company uses commercial paper to fund its day-to-day operations. Thus, any impairment of the Company's ability to issue commercial paper will increase the Company's borrowing costs, and therefore, its cost of service.

d. The information regarding the expected rate of interest is provided in Paragraph 3 of this Application.

e. Entering into the 5-1/4-Year RCA will enable the Company to access the lower-cost commercial paper market rather than having to rely on higher cost debt to fund its day-to-day operations. Information regarding the expected costs of the 5-1/4-Year RCA is provided in Paragraph 4 of this Application.

f. The impact of the proposed transaction on the Company's capital structure is nominal, as commercial paper supported by a long-term bank facility may be classified as long-term debt on the Company's Consolidated Balance Sheet.

Exhibit A

[K&S Draft 02/17/05]

Annex I

CAROLINA POWER & LIGHT COMPANY
D/B/A PROGRESS ENERGY CAROLINAS, INC.

$450,000,000 5-1/4 - Year Revolving Credit Facility

Borrower:	Carolina Power & Light Company, d/b/a Progress Energy Carolinas, Inc. (the "***Borrower***").
Amount and Type of Facility:	$450,000,000 5-1/4 - year unsecured revolving credit facility (the "***Facility***"). The size of the Facility may be increased during syndication, but in no event will exceed $________.
Purpose:	For general corporate purposes, including commercial paper backstop.
Administrative Agent:	Wachovia Bank, N.A. ("***Wachovia***" and, in its capacity as administrative agent, the "***Agent***").
Syndication Agent:	The Royal Bank of Scotland plc ("***RBS***").
Joint Lead Arrangers:	Wachovia Capital Markets, LLC and RBS Securities Corporation (the "***Arrangers***").
Lenders:	Wachovia, RBS and other financial institutions acceptable to the Borrower and the Agent.
Closing Date:	March [28], 2005, or such other date as may be agreed upon by the Borrower and the Arrangers.
Commitment Termination Date:	Five years and three months after the Closing Date.
Optional Commitment Reduction:	The Borrower will have the right, upon at least 3 business days' notice to the Agent, to terminate or cancel, in whole or in part, the unused portion of the Facility in excess of the aggregate outstanding Advances; *provided* that each partial reduction shall be in a minimum amount of $10,000,000 or any whole multiple of $1,000,000 in excess thereof. Once terminated, a commitment may not be reinstated.
Facility Fee:	Per the attached Pricing Grid, based on the Borrower's long-term senior unsecured non-credit-enhanced debt ratings, payable on each Lender's commitment, irrespective of usage, quarterly in arrears on the last day of each March, June, September and

December, and on the Commitment Termination Date.

The Facility Fee will be calculated on a 365/366-day basis.

Utilization Fee:	The amount per the attached Pricing Grid, based on the Borrower's long-term senior unsecured non-credit-enhanced debt ratings, by which the Applicable Margin will be increased upon usage of more than 50% of the commitments.
Interest Rates and Interest Periods:	At the Borrower's option, any Advance that is made to it will be available at the rates and for the Interest Periods stated below: (i) Base Rate: a fluctuating rate equal to the sum of (A) the higher of (x) Wachovia's Prime Rate and (y) the Federal Funds Rate plus ½% and (B) the Applicable Margin. (ii) Eurodollar Rate: a periodic fixed rate equal to LIBOR plus the Applicable Margin. The Eurodollar Rate will be fixed for Interest Periods of 1, 2, 3 or 6 months. Upon the occurrence and during the continuance of any Event of Default, each Eurodollar Rate Advance will convert to a Base Rate Advance at the end of the Interest Period then in effect for such Eurodollar Rate Advance.
Applicable Margin:	The Applicable Margin means an amount that will vary per the attached Pricing Grid, based on the Borrower's long-term senior unsecured non-credit-enhanced debt ratings. Upon the occurrence and during the continuance of any Event of Default, the Applicable Margin will increase by 200 basis points per annum.
Reference Banks:	Wachovia and certain other Lenders to be determined.
Interest Payments:	At the end of each calendar quarter for Base Rate Advances and at the end of each Interest Period for each Eurodollar Rate Advance, but no less frequently than quarterly. Interest will be computed on a 365/366-day basis for Base Rate Advances and a 360-day basis for Eurodollar Rate Advances.
Borrowings:	Borrowings will be in minimum principal amounts of $10,000,000 and integral multiples of $1,000,000 in excess thereof. All Advances will be made by the Lenders ratably in proportion to their respective commitments. Borrowings will be available on same day notice for Base Rate Advances and 3 business days'

notice for Eurodollar Rate Advances.

Availability: From the Closing Date and prior to the Commitment Termination Date, the Borrower may, subject to the terms of the Facility, borrow, repay and reborrow.

Repayment: The Borrower will repay each Advance no later than on the Commitment Termination Date.

Optional Prepayment: Advances may be prepaid without penalty, on same day notice for Base Rate Advances and 2 business days' notice for Eurodollar Rate Advances, in minimum amounts of $5,000,000 and increments of $1,000,000 in excess thereof. The Borrower will bear all costs related to the prepayment of a Eurodollar Rate Advance prior to the last day of the Interest Period.

Loan Documentation: The commitments will be subject to preparation, execution and delivery of mutually acceptable loan documentation that will contain conditions precedent, representations and warranties, covenants, events of default and other provisions customary for facilities of this nature, including, but not limited to, those noted below.

Conditions Precedent to Closing: Customary for facilities of this nature, including, but not limited to:

(1) Notes, if requested by any Lender.

(2) Board resolutions.

(3) Incumbency/specimen signature certificate.

(4) Certified copies of all necessary governmental approvals.

(5) Favorable legal opinion from counsel for the Borrower.

(6) Favorable legal opinion from counsel for the Agent.

(7) Accuracy of representations and warranties.

(8) The commitments under (i) the $165,000,000 364-Day Credit Agreement, dated as of April 1, 2003, among the Borrower, the lenders party thereto and JPMorgan Chase Bank, as administrative agent, and (ii) the $285,000,000 Three-Year Credit Agreement, dated as of July 31, 2002, among the Borrower, the lenders party thereto and Citibank, N.A., as administrative agent, shall have been terminated and all amounts outstanding under such facilities shall have been paid in full.

Conditions Precedent to all Advances:	Customary for facilities of this nature, including, but not limited to: (1) All representations and warranties (other than as described in item (6) below under "***Representations and Warranties***") are true and correct in all material respects on and as of the date of the Borrowing, before and after giving effect to such Borrowing and to the application of the proceeds therefrom, as though made on and as of such date. (2) No Event of Default or event that, with the giving of notice or passage of time or both, would be an Event of Default has occurred and is continuing or would result from such Borrowing.
Representations and Warranties:	Customary for facilities of this nature, including, but not limited to: (1) Confirmation of corporate status and authority. (2) Due authorization of the loan documents. (3) Execution, delivery and performance of loan documents do not violate law or existing agreements. (4) No governmental or regulatory approvals required, other than those that have been already duly issued, are final and in full force and effect. (5) No litigation which would have a material adverse effect on the financial condition, operations or properties of the Borrower and its Significant Subsidiaries, taken as a whole. (6) No material adverse change in the financial condition, operations or properties of the Borrower and its Significant Subsidiaries, taken as a whole, since December 31, 2003. (7) Accuracy and completeness of information and historical financial statements, subject to the effect (if any) of the Accounting Change. As used herein, "***Accounting Change***" means the application by the Borrower of a new accounting methodology for outage and emergency activities and indirect capital accounts, described in the Borrower's Current Report on Form 8-K filed with the Securities and Exchange Commission on December 16, 2004, which could result in certain costs for outage and emergency activities being expensed, rather than capitalized, during 2003 and/or prior years. (8) Material compliance with laws and regulations, including ERISA and all applicable environmental laws and regulations.

(9) Legality, validity, binding effect and enforceability of the loan documents.

(10) Margin regulations.

(11) Not an investment company.

(12) Use of proceeds.

Financial Covenant:

Maintain at all times a ratio of Consolidated Indebtedness to Total Capitalization no greater than .65:1.0.

As used herein, "***Consolidated Indebtedness***" means the sum of the following for the Borrower and its consolidated subsidiaries: (i) any obligation of such person for borrowed money, (ii) any obligation of such person evidenced by a bond, debenture, note or other similar instrument, (iii) any obligation of such person to pay the deferred purchase price of property or services, except a trade account payable that arises in the ordinary course of business but only if and so long as the same is payable on customary trade terms, (iv) any obligation of such person as lessee under a capital lease, (v) any mandatorily redeemable stock of such person (the amount of such mandatorily redeemable stock to be determined for this purpose as the higher of the liquidation preference and the amount payable upon redemption of such mandatorily redeemable stock), (vi) any obligation of such person to purchase securities or other property that arises out of or in connection with the sale of the same or substantially similar securities or property, (vii) any non-contingent obligation of such person to reimburse any other person in respect of amounts paid under a letter of credit or other guaranty issued by such other person to the extent that such reimbursement obligation remains outstanding after it becomes non-contingent, (viii) any indebtedness of others secured by (or for which the holder of such Indebtedness has an existing right, contingent or otherwise, to be secured by) a mortgage, lien, pledge, charge or other encumbrance on any asset of such person, (ix) any liabilities in respect of unfunded vested benefits under plans covered by Title IV of ERISA and (x) any indebtedness of others guaranteed by such person.

As used herein, "***Total Capitalization***" means the sum of the value of the common stock, retained earnings and preferred and preference stock of the Borrower (in each case, determined in accordance with generally accepted accounting principles consistent with those applied in the preparation of the financial statements referred to under the Section "Representations and Warranties" herein *plus* Consolidated Indebtedness of the

Borrower.

Covenants: Customary for facilities of this nature, including, but not limited to:

(1) Preservation and maintenance of corporate existence.

(2) Material compliance with laws (including ERISA and applicable environmental laws).

(3) Payment of taxes.

(4) Payment of material obligations.

(5) Visitation and inspection rights.

(6) Maintenance of books and records.

(7) Maintenance of properties.

(8) Maintenance of insurance.

(9) Certain restrictions on liens.

(10) Certain restrictions on change of business, consolidations, mergers and sales of assets (but excluding sales of assets not exceeding $250,000,000 in the aggregate in any fiscal year of the Borrower).

(11) Certain reporting requirements.

(12) Use of proceeds.

Events of Default: Customary for facilities of this nature, including, but not limited to:

(1) Failure to pay principal when due and failure to pay interest, fees and other amounts within 5 business days of when due.

(2) Representations or warranties materially incorrect when made.

(3) Failure to comply with covenants (with notice and cure periods as applicable).

(4) Cross-default to payment defaults on principal aggregating $35,000,000 or to other events if the effect is to accelerate or permit acceleration of such debt.

(5) Unsatisfied judgment or order in excess of $35,000,000.

(6) Bankruptcy/insolvency.

(7) ERISA.

(8) Change of control events as follows: (i) any person or "group" (within the meaning of Section 13(d) or 14(d) of the Securities Exchange Act of 1934, as amended) shall, directly or indirectly, acquire beneficial ownership of or control over securities of Progress Energy, Inc., representing in excess of 30% of the combined voting power of all securities of Progress Energy, Inc. entitled to vote in the election of directors of Progress Energy, Inc. or (ii) Progress Energy, Inc. shall fail to own, directly or indirectly, 95% of all securities of the Borrower entitled to vote in the election of directors of the Borrower.

Other:

Loan documentation will include:

(1) Indemnification of the Agent, the Arrangers, the Syndication Agent and the Lenders and each of their respective affiliates, officers, directors, employees, agents and advisors for any liabilities and expenses arising out of or in connection with the Facility or the use or proposed use of proceeds.

(2) Customary agency language.

(3) Majority Lenders defined as those holding greater than 50% of the principal amount of outstanding Advances or, if none, commitments. The consent of all the Lenders will be required to increase the size of the Facility, to extend the maturity or to decrease interest rates or fees.

Assignments and Participations:

Each Lender will have the right to assign to one or more eligible assignees all or a portion of its rights and obligations under the loan documents, with the consent, not to be unreasonably withheld, of the Agent and the Borrower; *provided* that the consent of the Borrower shall not be required if an Event of Default or event that, with the giving of notice or the passage of time, or both, would constitute an Event of Default shall have occurred and is continuing. Minimum aggregate assignment level of $5,000,000 and increments of $1,000,000 in excess thereof. The parties to the assignment (other than the Agent and the Borrower) will pay to the Agent an administrative fee of $3,500.

Each Lender will also have the right, without the consent of the Borrower or the Agent, to assign (i) as security, all or part of its rights under the loan documents to any Federal Reserve Bank and (ii) with notice to the Borrower and the Agent, all or part of its rights and obligations under the loan documents to any of its affiliates, any other Lender or any approved fund.

Each Lender will have the right to sell participations in its rights and obligations under the loan documents, subject to customary restrictions on the participant's voting rights.

Yield Protection, Taxes and Other Deductions:

(1) The loan documents will contain yield protection provisions, customary for facilities of this nature, protecting the Lenders in the event of unavailability of funding, funding losses, reserve requirements and changes in capital adequacy requirements.

(2) All payments to be free and clear of any present or future taxes, withholdings or other deductions whatsoever (other than income taxes in the jurisdiction of the Lender's organization or applicable lending office). The Lenders will use reasonable efforts to minimize to the extent possible any applicable taxes and the Borrower will indemnify the Lenders and the Agent for such taxes paid by the Lenders or the Agent.

The Borrower will have the right to replace any Lender that requests reimbursements for amounts owing under (1) above; *provided that* (i) no Event of Default, or event that, with the giving of notice or lapse of time, or both, would be an Event of Default, has occurred and is continuing, (ii) the Borrower has satisfied all of its obligations under the Facility relating to such Lender, and (iii) any replacement is acceptable to the Agent and the Borrower has paid the Agent a $3,500 administrative fee if such replacement Lender is not an existing lender.

Governing Law:

State of New York.

Submission to Jurisdiction and Waiver of Jury Trial:

The Borrower will submit to the jurisdiction of New York state and federal courts and will waive all rights to trial by jury.

Counsel to the Arrangers and the Agent:

King & Spalding LLP.

Expenses:

The Borrower will reimburse the Arrangers and the Agent for all reasonable out-of-pocket expenses (including fees and expenses of counsel to the Arrangers) incurred by them in the negotiation, syndication and execution of the Facility. Such expenses will be reimbursed by the Borrower upon presentation of a statement of account, regardless of whether the transaction contemplated is actually completed or the loan documents are signed.

CAROLINA POWER & LIGHT COMPANY
d/b/a Progress Energy Carolinas, Inc.
$450,000,000 5 ¼-Year Revolving Credit Facility
Pricing Grid

BASIS FOR PRICING	**LEVEL 1** Reference Ratings At Least A By S&P or A2 By Moody's	**LEVEL 2** Reference Ratings Less Than Level 1 But At Least A- By S&P or A3 By Moody's	**LEVEL 3** Reference Ratings Less Than Level 2 But At Least BBB+ By S&P or Baa1 By Moody's	**LEVEL 4** Reference Ratings Less Than Level 3 But At Least BBB By S&P or Baa2 By Moody's	**LEVEL 5** Reference Ratings Less Than Level 4 But At Least BBB- By S&P or Baa3 by Moody's	**LEVEL 6** Reference Ratings Less Than Level 5 or Unrated
Facility Fee(1)	8.0 bps	10.0 bps	12.5 bps	15.0 bps	17.5 bps	25.0 bps
Applicable Margin For Base Rate Advances	0.0 bps	0.0 bps	0.0 bps	0.0 bps	0.0 bps	0.0 bps
Applicable Margin For Eurodollar Advances	27.0 bps	27.5 bps	37.5 bps	45.0 bps	57.5 bps	75.0 bps
Utilization Fee(2)	12.5 bps	12.5 bps	12.5 bps	12.5 bps	12.5 bps	12.5 bps

"***Reference Ratings***" means the ratings assigned by Standard & Poor's ("***S&P***") and Moody's to the long-term unsecured senior, non-credit enhanced debt ratings of the Borrower. The Facility Fees, the Applicable Margins and the Utilization Fees shall be, at any time, the rate per annum set forth in the above table (expressed as basis points) below the relevant Reference Ratings. In the case of a split rating of one level, the higher rating will apply. In the case of a split rating of two or more levels, the rating that is one below the higher rating will apply.

(1) Paid quarterly in arrears on each bank's commitment irrespective of usage.

(2) If usage >50%.

INDEPENDENT AUDITORS' REPORT

TO THE BOARD OF DIRECTORS AND SHAREHOLDERS OF CAROLINA POWER & LIGHT COMPANY d/b/a PROGRESS ENERGY CAROLINAS, INC.:

We have audited the accompanying consolidated balance sheets of Carolina Power & Light Company d/b/a Progress Energy Carolinas, Inc. and its subsidiaries (PEC) at December 31, 2003 and 2002, and the related consolidated statements of income and comprehensive income, retained earnings, and cash flows for each of the three years in the period ended December 31, 2003. These financial statements are the responsibility of PEC's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of PEC at December 31, 2003 and 2002, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2003, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Notes 3F and 12A to the consolidated financial statements, in 2003, the Company adopted Statement of Financial Accounting Standards No. 143 and Derivative Implementation Group Issue C20.

/s/ DELOITTE & TOUCHE LLP
Raleigh, North Carolina
February 20, 2004

CAROLINA POWER & LIGHT COMPANY
d/b/a PROGRESS ENERGY CAROLINAS, INC.
CONSOLIDATED STATEMENTS of INCOME and COMPREHENSIVE INCOME

(In millions)	Years ended December 31 2003	2002	2001
Operating Revenues			
Electric	**$ 3,589**	$ 3,539	$ 3,344
Diversified business	**11**	15	16
Total Operating Revenues	**3,600**	3,554	3,360
Operating Expenses			
Fuel used in electric generation	**825**	752	638
Purchased power	**296**	347	354
Operation and maintenance	**782**	802	711
Depreciation and amortization	**562**	524	522
Taxes other than on income	**162**	158	150
Diversified business	**4**	15	10
Impairment of diversified business long-lived assets	**-**	101	-
Total Operating Expenses	**2,631**	2,699	2,385
Operating Income	**969**	855	975
Other Income (Expense)			
Interest income	**6**	7	14
Impairment of investments	**(21)**	(25)	(157)
Other, net	**(11)**	13	(4)
Total Other Expense	**(26)**	(5)	(147)
Interest Charges			
Interest charges	**196**	217	257
Allowance for borrowed funds used during construction	**(2)**	(5)	(16)
Total Interest Charges, Net	**194**	212	241
Income before Income Tax and Cumulative Effect of Change in Accounting Principles	**749**	638	587
Income Tax Expense	**244**	207	223
Income before Cumulative Effect of Change in Accounting Principles	**505**	431	364
Cumulative Effect of Change in Accounting Principles, Net of Tax	**(23)**	-	-
Net Income	**482**	431	364
Preferred Stock Dividend Requirement	**3**	3	3
Earnings for Common Stock	**$ 479**	$ 428	$ 361
Comprehensive Income, Net of Tax:			
Net Income	**$ 482**	$ 431	$ 364
SFAS No. 133 transition adjustment (net of tax)	**-**	-	(1)
Change in net unrealized losses on cash flow hedges (net of tax of ($1), $9 and $8, respectively)	**3**	(14)	(12)
Reclassification adjustment for amounts included in net income (net of tax of $0, $8 and $4, respectively)	**1**	11	6
Minimum pension liability adjustment (net of tax of $(47) and $47, respectively)	**72**	(73)	-
Comprehensive Income	**$ 558**	$ 355	$ 357

See Notes to Consolidated Financial Statements.

CAROLINA POWER & LIGHT COMPANY
d/b/a PROGRESS ENERGY CAROLINAS, INC.
CONSOLIDATED BALANCE SHEETS

(In millions)	December 31	
ASSETS	**2003**	2002
Utility Plant		
Utility plant in service	**$ 13,331**	$ 12,680
Accumulated depreciation	**(5,280)**	(4,869)
Utility plant in service, net	**8,051**	7,811
Held for future use	**5**	7
Construction work in progress	**306**	326
Nuclear fuel, net of amortization	**159**	177
Total Utility Plant, Net	**8,521**	8,321
Current Assets		
Cash and cash equivalents	**238**	18
Accounts receivable	**265**	301
Unbilled accounts receivable	**145**	151
Receivables from affiliated companies	**27**	37
Notes receivable from affiliated companies	**-**	50
Taxes receivable	**19**	55
Inventory	**348**	343
Deferred fuel cost	**113**	146
Prepayments and other current assets	**63**	45
Total Current Assets	**1,218**	1,146
Deferred Debits and Other Assets		
Regulatory assets	**477**	206
Nuclear decommissioning trust funds	**505**	423
Miscellaneous other property and investments	**169**	219
Other assets and deferred debits	**118**	90
Total Deferred Debits and Other Assets	**1,269**	938
Total Assets	**$ 11,008**	$ 10,405
CAPITALIZATION AND LIABILITIES		
Common Stock Equity		
Common stock without par value, authorized 200 million shares, 160 million shares issued and outstanding at December 31	**$ 1,953**	$ 1,930
Unearned ESOP common stock	**(89)**	(102)
Accumulated other comprehensive loss	**(7)**	(83)
Retained earnings	**1,380**	1,344
Total Common Stock Equity	**3,237**	3,089
Preferred Stock - Not Subject to Mandatory Redemption	**59**	59
Long-Term Debt	**3,086**	3,048
Total Capitalization	**6,382**	6,196
Current Liabilities		
Current portion of long-term debt	**300**	-
Accounts payable	**188**	258
Payables to affiliated companies	**136**	99
Notes payable to affiliated companies	**25**	-
Interest accrued	**64**	59
Short-term obligations	**4**	438
Current portion of accumulated deferred income taxes	**-**	66
Other current liabilities	**166**	92
Total Current Liabilities	**883**	1,012
Deferred Credits and Other Liabilities		
Accumulated deferred income taxes	**1,125**	1,105
Accumulated deferred investment tax credits	**148**	159
Regulatory liabilities	**1,175**	8
Cost of removal	**-**	1,488
Asset retirement obligations	**932**	-
Other liabilities and deferred credits	**363**	437
Total Deferred Credits and Other Liabilities	**3,743**	3,197
Commitments and Contingencies (Note 16)		
Total Capitalization and Liabilities	**$ 11,008**	$ 10,405

See Notes to Consolidated Financial Statements.

CAROLINA POWER & LIGHT COMPANY
d/b/a PROGRESS ENERGY CAROLINAS, INC.
CONSOLIDATED STATEMENTS of CASH FLOWS

(In millions)	Years ended December 31 **2003**	2002	2001
Operating Activities			
Net income	**$ 482**	$ 431	$ 364
Adjustments to reconcile net income to net cash provided by operating activities:			
Impairment of long-lived assets and investments	**21**	126	157
Depreciation and amortization	**660**	631	616
Cumulative effect of change in accounting principles	**23**	-	-
Deferred income taxes	**(68)**	(82)	(150)
Investment tax credit	**(10)**	(12)	(15)
Deferred fuel cost (credit)	**33**	(15)	(12)
Cash provided (used) by changes in operating assets and liabilities:			
Accounts receivable	**41**	(21)	304
Inventories	**4**	10	(140)
Prepayments and other current assets	**21**	(15)	22
Accounts payable	**(32)**	20	(261)
Other current liabilities	**56**	(2)	53
Other	**27**	32	47
Net Cash Provided by Operating Activities	**1,258**	1,103	985
Investing Activities			
Gross property additions	**(470)**	(624)	(824)
Proceeds from sale of assets and investments	**26**	244	-
Diversified business property additions and acquisitions	**(1)**	(12)	(13)
Nuclear fuel additions	**(66)**	(81)	(73)
Net contributions to nuclear decommissioning trust	**(31)**	(31)	(31)
Other investing activities	**1**	(17)	(32)
Net Cash Used in Investing Activities	**(541)**	(521)	(973)
Financing Activities			
Proceeds from issuance of long-term debt	**588**	542	296
Net increase (decrease) in short-term obligations	**(437)**	177	(226)
Net change in intercompany notes	**74**	(97)	188
Retirement of long-term debt	**(276)**	(807)	(135)
Equity contribution from parent	**-**	-	115
Dividends paid to parent	**(443)**	(397)	(256)
Dividends paid on preferred stock	**(3)**	(3)	(3)
Net Cash Used in Financing Activities	**(497)**	(585)	(21)
Net Increase (Decrease) in Cash and Cash Equivalents	**220**	(3)	(9)
Cash and Cash Equivalents at Beginning of Year	**18**	21	30
Cash and Cash Equivalents at End of Year	**$ 238**	$ 18	$ 21
Supplemental Disclosures of Cash Flow Information			
Cash paid during the year – interest (net of amount capitalized)	**$ 184**	$ 208	$ 230
income taxes (net of refunds)	**$ 296**	$ 319	$ 395

Noncash Investing and Financing Activities

- In January 2001, PEC transferred certain assets, through a noncash dividend to Progress Energy in the amount of $18 million, to Progress Energy Service Company, LLC.

See Notes to Consolidated Financial Statements.

CAROLINA POWER & LIGHT COMPANY
d/b/a PROGRESS ENERGY CAROLINAS, INC.
CONSOLIDATED STATEMENTS of RETAINED EARNINGS

(In millions)		Years ended December 31	
	2003	2002	2001
Retained Earnings at Beginning of Year	**$ 1,344**	$ 1,313	$ 1,226
Net income	**482**	431	364
Preferred stock dividends at stated rates	**(3)**	(3)	(3)
Common stock dividends	**(443)**	(397)	(274)
Retained Earnings at End of Year	**$ 1,380**	$ 1,344	$ 1,313

CONSOLIDATED QUARTERLY FINANCIAL DATA (UNAUDITED)

(In millions)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Year ended December 31, 2003				
Operating revenues	**$ 929**	**$ 819**	**$ 1,012**	**$ 840**
Operating income	**256**	**184**	**294**	**235**
Income before cumulative effect of change in accounting principles	**135**	**89**	**158**	**123**
Net income	**135**	**89**	**158**	**100**
Year ended December 31, 2002				
Operating revenues	$ 815	$ 838	$ 1,049	$ 852
Operating income	193	210	240	212
Net income	85	131	94	121

- In the opinion of management, all adjustments necessary to fairly present amounts shown for interim periods have been made. Results of operations for an interim period may not give a true indication of results for the year.
- Fourth quarter 2003 includes impairment of investments of $21 million ($13 million after-tax) (See Note 6).
- Fourth quarter 2003 includes a cumulative effect for DIG Issue C20 of $38 million ($23 million after-tax) (See Note 12).
- Third quarter 2002 includes impairment and other charges related to Caronet and Interpath Communications, Inc. of $133 million ($87 million, after-tax) (See Note 6).

See Notes to Consolidated Financial Statements.

CAROLINA POWER & LIGHT COMPANY
d/b/a PROGRESS ENERGY CAROLINAS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Organization and Summary of Significant Accounting Policies

A. Organization

Carolina Power & Light Company (CP&L) is a public service corporation primarily engaged in the generation, transmission, distribution and sale of electricity in portions of North Carolina and South Carolina. Effective January 1, 2003, CP&L began doing business under the assumed name Progress Energy Carolinas, Inc (PEC). The legal name has not changed and there is no restructuring of any kind related to the name change. Through its wholly-owned subsidiaries, PEC is involved in several nonregulated business activities, the most significant of which was its telecommunications operation. PEC is a wholly-owned subsidiary of Progress Energy, Inc. (the Company or Progress Energy). The Company is a registered holding company under the Public Utility Holding Company Act of 1935 (PUHCA). Both the Company and its subsidiaries are subject to the regulatory provisions of PUHCA.

In December 2003, Progress Telecommunications Corporation (PTC) and Caronet, Inc. (Caronet), both indirectly wholly-owned subsidiaries of Progress Energy, and EPIK Communications, Inc. (EPIK), a wholly-owned subsidiary of Odyssey Telecorp, Inc. (Odyssey), contributed substantially all of their assets and transferred certain liabilities to Progress Telecom, LLC (PTC LLC), a subsidiary of PTC. Subsequently, the stock of Caronet was sold to an affiliate of Odyssey for $2 million in cash and Caronet became an indirect wholly-owned subsidiary of Odyssey. No gain or loss was recognized on this transaction.

B. Basis of Presentation

The consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) and include the activities of PEC and its majority-owned subsidiaries. Significant intercompany balances and transactions have been eliminated in consolidation except as permitted by Statement of Financial Accounting Standards (SFAS) No. 71, "Accounting for the Effects of Certain Types of Regulation," which provides that profits on intercompany sales to regulated affiliates are not eliminated if the sales price is reasonable and the future recovery of the sales price through the ratemaking process is probable.

Unconsolidated investments in companies over which PEC does not have control, but has the ability to exercise influence over operating and financial policies (generally, 20% - 50% ownership), are accounted for under the equity method of accounting. Certain investments in debt and equity securities that have readily determinable market values, and for which PEC does not have control, are accounted for at fair value in accordance with SFAS No. 115 "Accounting for Certain Investments in Debt and Equity Securities." Other investments are stated principally at cost. These equity and cost investments, which total approximately $35 million and $95 million at December 31, 2003 and 2002, respectively, are included as miscellaneous property and investments in the Consolidated Balance Sheets. The primary component of this balance is PEC's investments in affordable housing of $21 million and $63 million at December 31, 2003 and 2002, respectively. This decrease is primarily due to the sale of certain PEC investments in the third quarter of 2003. For a discussion of how new FASB interpretations will affect these affordable housing investments see Note 2.

Certain amounts for 2002 and 2001 have been reclassified to conform to the 2003 presentation.

A. Significant Accounting Policies

Use of Estimates and Assumptions
In preparing consolidated financial statements that conform with GAAP, management must make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the consolidated financial statements and amounts of revenues and expenses reflected during the reporting period. Actual results could differ from those estimates.

Revenue Recognition
PEC recognizes electric utility revenue as service is rendered to customers. Operating revenues include unbilled electric utility revenues earned when service has been delivered but not billed by the end of the accounting period. Revenues related to Caronet for the design and construction of wireless infrastructure were recognized upon completion of services for each completed phase of design and construction.

Fuel Cost Deferrals
Fuel expense includes fuel costs or recoveries that are deferred through fuel clauses established by PEC's regulators. These clauses allow PEC to recover fuel costs and portions of purchased power costs through surcharges on customer rates.

Excise Taxes
PEC collects from customers certain excise taxes levied by the state or local government upon the customer. PEC accounts for excise taxes on a gross basis. For the years ended December 31, 2003, 2002 and 2001, gross receipts tax and other excise taxes of approximately $81 million, $79 million and $77 million, respectively, are included in taxes other than on income on the Consolidated Statements of Income and Comprehensive Income. These approximate amounts also are included in electric operating revenues.

Income Taxes
Progress Energy and its affiliates file a consolidated federal income tax return. The consolidated income tax of Progress Energy is allocated to PEC in accordance with the Inter-company Income Tax Allocation Agreement (Tax Agreement). The Tax Agreement provides an allocation that recognizes positive and negative corporate taxable income. The Tax Agreement provides for an equitable method of apportioning the carry over of uncompensated tax benefits. Progress Energy tax benefits not related to acquisition interest expense are allocated to profitable subsidiaries, beginning in 2002, in accordance with a PUHCA order. Income taxes are provided as if PEC filed a separate return.

Deferred income taxes have been provided for temporary differences. These occur when there are differences between the book and tax carrying amounts of assets and liabilities. Investment tax credits related to regulated operations have been deferred and are being amortized over the estimated service life of the related properties (See Note 10).

Stock-Based Compensation
The Company measures compensation expense for stock options as the difference between the market price of its common stock and the exercise price of the option at the grant date. The exercise price at which options are granted by the Company equals the market price at the grant date, and accordingly no compensation expense has been recognized for stock option grants. For purposes of the pro forma disclosures required by SFAS No. 148, "Accounting for Stock-Based Compensation – Transition and Disclosure – an Amendment of FASB Statement No. 123" (SFAS No. 148), the estimated fair value of the Company's stock options is amortized to expense over the options' vesting period. The following table illustrates the effect on net income if the fair value method had been applied to all outstanding and unvested awards in each period.

(in millions)	**2003**	2002	2001
Net income, as reported	**$ 482**	$ 431	$ 364
Deduct: Total stock option expense determined under fair value method for all awards, net of related tax effects	**6**	5	1
Pro forma net income	**$ 476**	$ 426	$ 363

Utility Plant
Utility plant in service is stated at historical cost less accumulated depreciation. PEC capitalizes all construction-related direct labor and material costs of units of property as well as indirect construction costs. The cost of renewals and betterments is also capitalized. Maintenance and repairs of property, and replacements and renewals of items determined to be less than units of property, are charged to maintenance expense as incurred. The cost of units of property replaced or retired, less salvage, is charged to accumulated depreciation. Removal or disposal costs were charged to regulatory liabilities in 2003 and cost of removal in 2002. PEC follows the guidance in SFAS No. 143, "Accounting for Asset Retirement Obligations," to account for legal obligations associated with the retirement of certain tangible long-lived assets.

Depreciation and Amortization – Utility Plant
For financial reporting purposes, substantially all depreciation of utility plant other than nuclear fuel is computed on the straight-line method based on the estimated remaining useful life of the property, adjusted for estimated salvage (See Note 3A). The North Carolina Utilities Commission (NCUC) and the Public Service Commission of South Carolina (SCPSC) can also grant approval to accelerate or reduce depreciation and amortization of utility assets (See Note 5B).

Amortization of nuclear fuel costs, including disposal costs associated with obligations to the U.S. Department of Energy (DOE) and costs associated with obligations to the DOE for the decommissioning and decontamination of enrichment facilities, is computed primarily on the units-of-production method and charged to fuel used in electric generation in the accompanying Consolidated Statements of Income and Comprehensive Income. In PEC's retail jurisdictions, provisions for nuclear decommissioning costs are approved by the NCUC and the SCPSC and are based on site-specific estimates that include the costs for removal of all radioactive and other structures at the site. In the wholesale jurisdictions, the provisions for nuclear decommissioning costs are approved by the Federal Energy Regulatory Commission (FERC).

Cash and Cash Equivalents
PEC considers cash and cash equivalents to include unrestricted cash on hand, cash in banks and temporary investments purchased with a maturity of three months or less.

Allowance for Doubtful Accounts
PEC maintains an allowance for doubtful accounts receivable, which totaled approximately $13 million and $11 million at December 31, 2003 and 2002, respectively, and is included in accounts receivable on the Consolidated Balance Sheets.

Inventory
PEC accounts for inventory using the average-cost method.

Regulatory Assets and Liabilities
PEC's regulated operations are subject to SFAS No. 71, which allows a regulated company to record costs that have been or are expected to be allowed in the ratemaking process in a period different from the period in which the costs would be charged to expense by a nonregulated enterprise. Accordingly, PEC records assets and liabilities that result from the regulated ratemaking process that would not be recorded under GAAP for nonregulated entities. These regulatory assets and liabilities represent expenses deferred for future recovery from customers or obligations to be refunded to customers and are primarily classified in the accompanying Consolidated Balance Sheets as regulatory assets and regulatory liabilities (See Note 5A).

Diversified Business Property
Diversified business property is stated at cost less accumulated depreciation. If an impairment loss is recognized on an asset, the fair value becomes its new cost basis. The costs of renewals and betterments are capitalized. The cost of repairs and maintenance is charged to expense as incurred. Depreciation is computed on a straight-line basis using the estimated useful lives disclosed in Note 3B.

Unamortized Debt Premiums, Discounts and Expenses
Long-term debt premiums, discounts and issuance expenses for the utility are amortized over the life of the related debt using the straight-line method. Any expenses or call premiums associated with the reacquisition of debt obligations by the utility are amortized over the remaining life of the original debt using the straight-line method consistent with ratemaking treatment.

Derivatives
Effective January 1, 2001, PEC adopted SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" (SFAS No. 133), as amended by SFAS No. 138 and SFAS No. 149. SFAS No. 133, as amended, establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. SFAS No. 133 requires that an entity recognize all derivatives as assets or liabilities in the balance sheet and measure those instruments at fair value. During 2003, the FASB reconsidered an interpretation of SFAS No. 133. See Note 12 for the effect of the interpretation and additional information regarding risk management activities and derivative transactions.

Environmental
The Company accrues environmental remediation liabilities when the criteria for SFAS No. 5, "Accounting for Contingencies," has been met. Environmental expenditures are expensed as incurred or capitalized depending on their future economic benefit. Expenditures that relate to an existing condition caused by past operations and that have no future economic benefits are expensed. Accruals for estimated losses from environmental remediation obligations generally are recognized no later than completion of the remedial feasibility study. Such accruals are adjusted as additional information develops or circumstances change. Costs of future expenditures for environmental remediation obligations are not discounted to their present value. Recoveries of environmental remediation costs from other parties are recognized when their receipt is deemed probable (See Note 16D).

Impairment of Long-lived Assets and Investments
The Company reviews the recoverability of long-lived tangible and intangible assets whenever indicators exist. Examples of these indicators include current period losses, combined with a history of losses or a projection of continuing losses, or a significant decrease in the market price of a long-lived asset group. If an indicator exists, then the asset group is tested for recoverability by comparing the carrying value to the sum of undiscounted expected future cash flows directly attributable to the asset group. If the asset group is not recoverable through undiscounted cash flows, then an impairment loss is recognized for the difference between the carrying value and the fair value of the asset group. The accounting for impairment of long-lived assets is based on SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," which was adopted by the Company effective January 1, 2002. Prior to the adoption of this standard, impairments were accounted for under SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of" (SFAS No. 121), which was superceded by SFAS No. 144.

PEC reviews its investments to evaluate whether or not a decline in fair value below the carrying value is an other-than-temporary decline. PEC considers various factors, such as the investee's cash position, earnings and revenue outlook, liquidity and management's ability to raise capital in determining whether the decline is other-than-temporary. If PEC determines that an other-than-temporary decline exists in the value of its investments, it is PEC's policy to write-down these investments to fair value. See Note 6 for a discussion of impairment evaluations performed and charges taken.

Subsidiary Stock Transactions
Gains and losses realized as a result of common stock sales by PEC's subsidiaries are recorded in the Consolidated Statements of Income and Comprehensive Income, except for any transactions that must be credited directly to equity in accordance with the provisions of SAB No. 51, "Accounting for Sales of Stock by a Subsidiary."

2. New Accounting Standards

SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity"
In May 2003, the Financial Accounting Standards Board (FASB) issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity." The adoption of SFAS No. 150 did not have an impact on PEC's financial position or results of operations.

EITF Issue No. 03-04, "Accounting for 'Cash Balance' Pension Plans"
In May 2003, the Emerging Issues Task Force (EITF) reached consensus in EITF Issue No. 03-04, "Accounting for 'Cash Balance' Pension Plans" (EITF 03-04), to specifically address the accounting for certain cash balance pension plans. The consensus reached in EITF 03-04 requires certain cash balance pension plans to be accounted for as defined benefit plans. For cash balance plans described in EITF 03-04, the consensus also requires the use of the traditional unit credit method for purposes of measuring the benefit obligation and annual cost of benefits earned as opposed to the projected unit credit method. PEC has historically accounted for its cash balance plan as a defined benefit plan; however, PEC was required to adopt the measurement provisions of EITF 03-04 at its cash balance plan's measurement date of December 31, 2003. Any differences in the measurement of the obligations as a result of applying EITF 03-04 were reported as a component of actuarial gain or loss. The on-going effects of this standard are dependent on other factors that also affect the determination of actuarial gains and losses and the subsequent amortization of such gains and losses. However, the adoption of EITF 03-04 is not expected to have a material effect on PEC's results of operations or financial position.

SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities"

In April 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." The statement amends and clarifies SFAS No. 133 on accounting for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. The new guidance incorporates decisions made as part of the Derivatives Implementation Group (DIG) process, as well as decisions regarding implementation issues raised in relation to the application of the definition of a derivative. SFAS No. 149 is generally effective for contracts entered into or modified after June 30, 2003. Interpretations and implementation issues with regard to SFAS No. 149 continue to evolve. The statement had no significant impact on PEC's accounting for contracts entered into subsequent to the statement's effective date (See Note 12). Future effects, if any, on PEC's results of operations and financial condition will be dependent on the specifics of future contracts entered into with regard to guidance provided by the statement. In connection with the January 2003 FASB EITF meeting, the FASB was requested to reconsider an interpretation of SFAS No. 133 (See Note 12).

FIN No. 46, "Consolidation of Variable Interest Entities"

In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities – an Interpretation of ARB No. 51" (FIN No. 46). This interpretation provides guidance related to identifying variable interest entities and determining whether such entities should be consolidated. FIN No. 46 requires an enterprise to consolidate a variable interest entity when the enterprise (*a*) absorbs a majority of the variable interest entity's expected losses, (*b*) receives a majority of the entity's expected residual returns, or both, as a result of ownership, contractual or other financial interests in the entity. Prior to the effective date of FIN No. 46, entities were generally consolidated by an enterprise that had control through ownership of a majority voting interest in the entity. FIN No. 46 originally applied immediately to variable interest entities created or obtained after January 31, 2003. During 2003, PEC did not participate in the creation of, or obtain a new variable interest in, any variable interest entity. In December 2003, the FASB issued a revision to FIN No. 46 (FIN No. 46R), which modified certain requirements of FIN No. 46 and allowed for the optional deferral of the effective date of FIN No. 46R until March 31, 2004. However, entities subject to FIN No. 46 or FIN No. 46R that are deemed to be special-purpose entities (as defined in FIN No. 46R) must implement either FIN No. 46 or FIN No. 46R at December 31, 2003. PEC elected to apply FIN No. 46 to special purpose entities as of December 31, 2003. Because PEC expects additional transitional guidance to be issued, it has elected to apply FIN No. 46R to non-special-purpose entities as of March 31, 2004.

PEC has investments in 14 limited partnerships accounted for under the equity method for which it may be the primary beneficiary. These partnerships invest in and operate low-income housing and historical renovation properties that qualify for federal and state tax credits. PEC has not concluded whether it is the primary beneficiary of these partnerships. These partnerships are partially funded with financing from third party lenders, which is secured by the assets of the partnerships. The creditors of the partnerships do not have recourse to PEC. At December 31, 2003, the maximum exposure to loss as a result of PEC's investments in these limited partnerships is approximately $9 million. PEC expects to complete its evaluation of these partnerships under FIN No. 46R during the first quarter of 2004. If PEC had consolidated these 14 entities at December 31, 2003, it would have recorded an increase to both total assets and total liabilities of approximately $40 million.

PEC also has interests in several other variable interest entities created before January 31, 2003, for which it is not the primary beneficiary. These arrangements include equity investments in approximately 14 limited partnerships, limited liability corporations and venture capital funds, and two building leases with special-purpose entities. The aggregate maximum loss exposure at December 31, 2003 under these arrangements totals approximately $23 million. The creditors of these variable interest entities do not have recourse to the general credit of PEC in excess of the aggregate maximum loss exposure.

In February 2004, PEC became aware that certain long-term purchase power and tolling contracts may be considered variable interests under FIN No. 46R. PEC has various long-term purchase power and tolling contracts with other utilities and certain qualifying facility plants. PEC believes the counterparties to these contracts are not special-purpose entities and, therefore, FIN No. 46R would not apply to these contracts until March 31, 2004. PEC has not yet completed its evaluation of these contracts to determine if the Company needs to consolidate these counterparties under FIN No. 46R and will continue to monitor developing practice in this area.

3. Property, Plant and Equipment

A. Utility Plant

The balances of utility plant in service at December 31 are listed below, with a range of depreciable lives for each:

(in millions)	2003	2002
Production plant (7-33 years)	**$ 8,024**	$ 7,630
Transmission plant (30-75 years)	**1,155**	1,128
Distribution plant (12-50 years)	**3,538**	3,345
General plant and other (8-75 years)	**614**	577
Utility plant in service	**$ 13,331**	$ 12,680

Generally, electric utility plant, other than nuclear fuel is pledged as collateral for the first mortgage bonds of PEC (See Note 8).

Allowance for funds used during construction (AFUDC) represents the estimated debt and equity costs of capital funds necessary to finance the construction of new regulated assets. As prescribed in the regulatory uniform systems of accounts, AFUDC is charged to the cost of the plant. The equity funds portion of AFUDC is credited to other income and the borrowed funds portion is credited to interest charges. Regulatory authorities consider AFUDC an appropriate charge for inclusion in the rates charged to customers by the utilities over the service life of the property. The composite AFUDC rate for PEC's electric utility plant was 4.0% in 2003 and 6.2% in 2002 and 2001.

Depreciation provisions on utility plant, as a percent of average depreciable property other than nuclear fuel, were 2.7% in 2003 and 2002 and 2.5% in 2001. The depreciation provisions related to utility plant were $345 million, $326 million and $305 million in 2003, 2002 and 2001, respectively. In addition to utility plant depreciation provisions, depreciation and amortization expense also includes decommissioning cost provisions, asset retirement obligations (ARO) accretion, cost of removal provisions (See Note 3D) and regulatory approved expenses (See Note 5).

PEC filed a new depreciation study in 2004 that provides support for reducing depreciation expense on an annual basis by approximately $45 million. The reduction is primarily attributable to assumption changes for nuclear generation, offset by increases for distribution assets. The new rates are primarily effective January 1, 2004.

The amortization of nuclear fuel costs for the years ended December 31, 2003, 2002 and 2001 were $112 million, $109 million and $101 million, respectively.

B. Diversified Business Property

Gross diversified business property was $8 million and $10 million at December 31, 2003 and 2002, respectively. These amounts consist primarily of equipment which is being depreciated over periods ranging from 3 to 10 years. Accumulated depreciation was $1 million at December 31, 2003 and 2002. Diversified business depreciation expense was $1 million, $4 million and $6 million in 2003, 2002 and 2001, respectively. Net diversified business property is included in miscellaneous other property and investments on the Consolidated Balance Sheets.

C. Joint Ownership of Generating Facilities

PEC holds ownership interests in certain jointly owned generating facilities. PEC is entitled to shares of the generating capability and output of each unit equal to their respective ownership interests. PEC also pays its ownership share of additional construction costs, fuel inventory purchases and operating expenses. PEC's share of expenses for the jointly owned facilities is included in the appropriate expense category. PEC's ownership interest in the jointly-owned generating facilities is listed below with related information at December 31 ($ in millions):

Facility	Company Ownership Interest	Plant Investment	Accumulated Depreciation	Construction Work in Progress
2003				
Mayo Plant	**83.83%**	**$ 464**	**$ 242**	**$ 50**
Harris Plant	**83.83%**	**3,248**	**1,370**	**7**
Brunswick Plant	**81.67%**	**1,611**	**884**	**21**
Roxboro Unit No. 4	**87.06%**	**323**	**139**	**1**
2002				
Mayo Plant	83.83%	$ 464	$ 232	$ 14
Harris Plant	83.83%	3,160	1,331	6
Brunswick Plant	81.67%	1,477	811	26
Roxboro Unit No. 4	87.06%	316	134	8

In the tables above, plant investment and accumulated depreciation are not reduced by the regulatory disallowances related to the Shearon Harris Nuclear Plant (Harris Plant).

D. Decommissioning and Cost of Removal Provisions

Decommissioning cost provisions, which are included in depreciation and amortization expense, were $31 million in 2003, 2002 and 2001. Management believes that the decommissioning costs that have been and will be recovered through rates will be sufficient to provide for the costs of decommissioning.

PEC's cost of removal provisions, which are included in deprecation and amortization expense, were $86 million, $81 million and $77 million in 2003, 2002 and 2001, respectively. These amounts represent the expense recognized for the disposal or removal of utility assets. The FASB has issued SFAS No. 143, "Accounting for Asset Retirement Obligations" (SFAS No. 143), that changed the accounting for decommissioning and cost of removal provisions (See Note 3F).

E. Insurance

PEC is a member of Nuclear Electric Insurance Limited (NEIL), which provides primary and excess insurance coverage against property damage to members' nuclear generating facilities. Under the primary program, PEC is insured for $500 million at each of its nuclear plants. In addition to primary coverage, NEIL also provides decontamination, premature decommissioning and excess property insurance with limits of $2.0 billion on the Brunswick and Harris Plants and $1.1 billion on the Robinson Plant.

Insurance coverage against incremental costs of replacement power resulting from prolonged accidental outages at nuclear generating units is also provided through membership in NEIL. PEC is insured thereunder, following a twelve-week deductible period, for 52 weeks in the amount of $3 million per week at the Brunswick and Harris Plants and $2.5 million per week at the Robinson Plant. An additional 110 weeks of coverage is provided at 80% of the above weekly amounts. For the current policy period, PEC is subject to retrospective premium assessments of up to approximately $21 million with respect to the primary coverage, $25 million with respect to the decontamination, decommissioning and excess property coverage, and $14 million for the incremental replacement power costs coverage, in the event covered losses at insured facilities exceed premiums, reserves, reinsurance and other NEIL resources. Pursuant to regulations of the United States Nuclear Regulatory Commission (NRC), PEC's property damage insurance policies provide that all proceeds from such insurance be applied, first, to place the plant in a safe and stable condition after an accident and, second, to decontaminate, before any proceeds can be used for decommissioning, plant repair or restoration. PEC is responsible to the extent losses may exceed limits of the coverage described above.

PEC is insured against public liability for a nuclear incident up to $10.9 billion per occurrence. Under the current provisions of the Price Anderson Act, which limits liability for accidents at nuclear power plants, PEC, as an owner of nuclear units, can be assessed for a portion of any third-party liability claims arising from an accident at any commercial nuclear power plant in the United States. In the event that public liability claims from an insured nuclear incident exceed $300 million (currently available through commercial insurers), PEC would be subject to pro rata assessments of up to $101 million for each reactor owned per occurrence. Payment of such assessments would be made over time as necessary to limit the payment in any one year to no more than $10 million per reactor owned. Congress is expected to approve revisions to the Price Anderson Act during 2004 that could include increased limits and assessments per reactor owned. The final outcome of this matter cannot be predicted at this time.

Under the NEIL policies, if there were multiple terrorism losses occurring within one year, NEIL would make available one industry aggregate limit of $3.2 billion, along with any amounts it recovers from reinsurance, government indemnity or other sources up to the limits for each claimant. If terrorism losses occurred beyond the one-year period, a new set of limits and resources would apply. For nuclear liability claims arising out of terrorist acts, the primary level available through commercial insurers is now subject to an industry aggregate limit of $300 million. The second level of coverage obtained through the assessments discussed above would continue to apply to losses exceeding $300 million and would provide coverage in excess of any diminished primary limits due to the terrorist acts.

PEC self-insures its transmission and distribution lines against loss due to storm damage and other natural disasters.

F. Asset Retirement Obligations

SFAS No. 143 provides accounting and disclosure requirements for retirement obligations associated with long-lived assets and was adopted by the Company effective January 1, 2003. This statement requires that the present value of retirement costs for which PEC has a legal obligation be recorded as a liability with an equivalent amount added to the asset cost and depreciated over an appropriate period. The liability is then accreted over time by applying an interest method of allocation to the liability. Cumulative accretion and accumulated depreciation were recognized for the time period from the date the liability would have been recognized had the provisions of this statement been in effect to the date of adoption of this statement.

Upon adoption of SFAS No. 143, PEC recorded AROs for nuclear decommissioning of irradiated plant totaling $880 million. PEC used an expected cash flow approach to measure these obligations. This amount includes accruals recorded prior to adoption totaling $491 million, which were previously recorded in cost of removal. The related asset retirement costs, net of accumulated depreciation, recorded upon adoption totaled $117 million. The cumulative effect of adoption of this statement had no impact on the net income of PEC, as the effects were offset by the establishment of a regulatory asset in the amount of $271 million, pursuant to SFAS No. 71. The regulatory asset represents the cumulative accretion and accumulated depreciation for the time period from the date the liability would have been recognized had the provisions of this statement been in effect to the date of adoption, less the amount previously recorded.

The asset retirement costs related to nuclear decommissioning of irradiated plant, net of accumulated depreciation, totaled $113 million at December 31, 2003. The ongoing expense differences between SFAS No. 143 and regulatory cost recovery are being deferred to the regulatory asset.

Funds set aside in PEC's nuclear decommissioning trust fund for the nuclear decommissioning liability totaled $505 million at December 31, 2003 and $423 million at December 31, 2002. Net unrealized gains on the nuclear decommissioning trust fund were included in regulatory liabilities in 2003 and cost of removal in 2002.

The following table shows the changes to the asset retirement obligations during the year ended December 31, 2003:

(in millions)	
Asset retirement obligations as of January 1, 2003	$ 880
Accretion expense	52
Asset retirement obligations as of December 31, 2003	$ 932

Pro forma net income has not been presented for prior years because the pro forma application of SFAS No. 143 to prior years would result in pro forma net income not materially different from the actual amounts reported.

PEC has identified but not recognized AROs related to electric transmission and distribution and telecommunications assets as the result of easements over property not owned by PEC. These easements are generally perpetual and only require retirement action upon abandonment or cessation of use of the property for the specified purpose. The ARO liability is not estimable for such easements as PEC intends to utilize these properties indefinitely. In the event PEC decides to abandon or cease the use of a particular easement, an ARO liability would be recorded at that time.

PEC previously recognized removal and decommissioning costs as a component of accumulated depreciation in accordance with regulatory treatment. At December 31, 2003, such costs totaling $994 million were included in regulatory liabilities on the Consolidated Balance Sheet and consist of removal costs of $927 million and removal costs for non-irradiated areas at nuclear facilities of $67 million. At December 31, 2002, such costs totaling $1,488 million were included in cost of removal on the Consolidated Balance Sheet and consist of removal costs of $877 million and decommissioning costs for both the irradiated and non-irradiated areas at nuclear facilities of $611 million. With the adoption of SFAS No. 143 in 2003, removal costs related to the irradiated areas at nuclear facilities are reported as asset retirement obligations on the 2003 Consolidated Balance Sheet.

PEC filed a request with the NCUC requesting deferral of the difference between expense pursuant to SFAS No. 143 and expense as previously determined by the NCUC. The NCUC initially granted the deferral of the January 1, 2003 cumulative adjustment. During the third quarter of 2003, the NCUC issued an order allowing the deferral of the ongoing effects.

In April 2003, the SCPSC approved a joint request by PEC, Duke Energy Corporation and South Carolina Electric and Gas Company for an accounting order to authorize the deferral of all cumulative and prospective effects related to the adoption of SFAS No. 143.

Therefore, the actions of the NCUC and SCPSC had no impact on the income of PEC for the year ended December 31, 2003.

4. Inventory

At December 31, inventory was comprised of:

(in millions)	**2003**	2002
Fuel	**$ 118**	$ 118
Materials and supplies	**230**	225
Total inventory	**$ 348**	$ 343

5. Regulatory Matters

A. Regulatory Assets and Liabilities

As a regulated entity, PEC is subject to the provisions of SFAS No. 71. Accordingly, PEC records certain assets and liabilities resulting from the effects of the ratemaking process which would not be recorded under GAAP for nonregulated entities. PEC's ability to continue to meet the criteria for application of SFAS No. 71 may be affected in the future by competitive forces and restructuring in the electric utility industry. In the event that SFAS No. 71 no longer applied to a separable portion of PEC's operations, related regulatory assets and liabilities would be eliminated unless an appropriate regulatory recovery mechanism was provided. Additionally, these factors could result in an impairment of utility plant assets as determined pursuant to SFAS No. 144 (See Note 1C).

At December 31, the balances of PEC's regulatory assets (liabilities) were as follows:

(in millions)	2003	2002
Deferred fuel cost	$ 113	$ 146
Deferred impact of ARO (Note 3F)	291	-
Income taxes recoverable through future rates (Note 10)	94	122
Loss on reacquired debt (Note 1C)	22	13
Storm deferral (Note 5B)	21	-
Deferred DOE enrichment facilities-related costs (Note 1C)	19	25
Other	30	46
Total long-term regulatory assets	477	206
Non-ARO cost of removal (Note 3F)	(994)	-
Emission allowance	(8)	(8)
Net nuclear decommissioning trust unrealized gains (Note 3F)	(99)	-
Clean air compliance (Note 5B)	(74)	-
Total long-term regulatory liabilities	(1,175)	(8)
Net regulatory assets/(liabilities)	$ (585)	$ 344

Except for portions of deferred fuel, all assets earn a return or the cash has not yet been expended, in which case the assets are offset by liabilities that do not incur a carrying cost. The utility expects to fully recover these assets and refund the liabilities through customer rates under current regulatory practice.

B. Retail Rate Matters

The NCUC and SCPSC approved proposals to accelerate cost recovery of PEC's nuclear generating assets beginning January 1, 2000, and continuing through 2009. The aggregate minimum and maximum amounts of accelerated cost recovery are $530 million and $750 million, respectively. Accelerated cost recovery of these assets resulted in no additional expense in 2003 and additional depreciation expense of approximately $53 million and $75 million in 2002 and 2001, respectively. Total accelerated depreciation recorded through December 31, 2003 was $403 million.

In conjunction with the acquisition of NCNG in 1999, PEC agreed to cap base retail electric rates in North Carolina and South Carolina through December 2004. The cap on base retail electric rates in South Carolina was extended to December 2005 in conjunction with regulatory approval to form a holding company.

The NC Clean Air Act of June 2002 (the Clean Air Act), requires state utilities to reduce emissions of nitrogen oxide (NOx) and sulfur dioxide (SO2) from coal-fired plants. The NCUC has allowed the utilities to amortize and recover the costs associated with meeting the new emission standards over a seven-year period beginning January 1, 2003. PEC recognized $74 million of clean air amortization during 2003. This legislation freezes PEC's base rates in North Carolina for five years, subject to certain conditions (See Note 16D).

In conjunction with the Company's merger with Florida Progress Corporation (Florida Progress), PEC reached a settlement with the Public Staff of the NCUC in which it agreed to reduce rates to all of its non-real time pricing customers by $3 million in 2002, $5 million in 2003, and $6 million in both 2004 and 2005.

PEC obtained SCPSC and NCUC approval of fuel factors in annual fuel-adjustment proceedings. The SCPSC approved PEC's petition to leave billing rates unchanged from the prior year by order issued March 28, 2003. The NCUC approved an increase of $20 million by order issued September 25, 2003.

On October 16, 2003, PEC made a filing with the NCUC to seek permission to defer expenses incurred from Hurricane Isabel and the February 2003 winter storms. As a result of rising storm costs and the frequency of major storm damage, PEC asked the NCUC to allow PEC to create a deferred account in which PEC would place expenses incurred as a result of named tropical storms, hurricanes and significant winter storms. In December 2003, the NCUC approved PEC's request to defer the costs and amortize them over a period of 5 years beginning in the month the storm occurs. PEC charged approximately $24 million in 2003 from Hurricane Isabel and from current year ice storms to the deferred account, of which $3 million was amortized during 2003.

PEC retains funds internally to meet decommissioning liability. The NCUC order issued February 2004 found that by January 1, 2008 PEC must begin transitioning these amounts to external funds. The transition of $131 million must be completed by December 31, 2017, and at least 10% must be transitioned each year. PEC has exclusively utilized external funding for its decommissioning liability since 1994.

C. Regional Transmission Organizations and Standard Market Design

In 2000, the FERC issued Order No. 2000 on RTOs, which set minimum characteristics and eight functions for transmission entities, including independent system operators (ISOs) and transmission companies that are required to become FERC-approved RTOs. As a result of Order 2000, PEC, along with Duke Energy Corporation and South Carolina Electric & Gas Company, filed and received provisional approval from the FERC for a GridSouth RTO. However, in July 2001, the FERC issued orders recommending that companies in the Southeast engage in mediation to develop a plan for a single RTO for the Southeast. PEC participated in the mediation. The FERC has not issued an order specifically on this mediation.

In July 2002, the FERC issued its Notice of Proposed Rulemaking in Docket No. RM01-12-000, Remedying Undue Discrimination through Open Access Transmission Service and Standard Electricity Market Design (SMD NOPR). If adopted as proposed, the rules set forth in the SMD NOPR would materially alter the manner in which transmission and generation services are provided and paid for. PEC filed comments in November 2002 and supplement comments in January 2003. In April 2003, the FERC released a White Paper on the Wholesale Market Platform. The White Paper provides an overview of what the FERC currently intends to include in a final rule in the SMD NOPR docket. The White Paper retains the fundamental and most protested aspects of SMD NOPR, including mandatory RTOs and the FERC's assertion of jurisdiction over certain aspects of retail service. The FERC has not yet issued a final rule on SMD NOPR.

PEC has $33 million invested in GridSouth at December 31, 2003. Given the regulatory uncertainty of the ultimate timing, structure and operations of GridSouth, or an alternate combined transmission structure, PEC cannot predict the effect on future consolidated results of operations, cash flows or financial condition. Furthermore, the SMD NOPR presents several uncertainties, including what percentage of the investment in GridSouth will be recovered, how the elimination of transmission charges, as proposed in the SMD NOPR, will impact PEC, and what amount of capital expenditures will be necessary to create a new wholesale market.

6. Impairments of Long-Lived Assets and Investments

Effective January 1, 2002, PEC adopted SFAS No. 144, which provides guidance for the accounting and reporting of impairment or disposal of long-lived assets. The statement supersedes SFAS No. 121. In 2003, 2002 and 2001, PEC recorded pre-tax long-lived asset and investment impairments and other charges of approximately $21 million, $133 million and $157 million, respectively.

A. Long-Lived Assets

In 2002, PEC initiated an independent valuation study to assess the recoverability of Caronet's long-lived assets. Based on this assessment, PEC recorded asset impairments of $101 million on a pre-tax basis and other charges of $7 million on a pre-tax basis in the third quarter of 2002. This write-down constituted a significant reduction in the book value of these long-lived assets. The long-lived asset impairments included an impairment of property, plant and equipment, construction work in process and intangible assets. The impairment charge represents the difference between the fair value and carrying amount of these long-lived assets. The fair value of these assets was determined using a valuation study heavily weighted on the discounted cash flow methodology, while using market approaches as supporting information.

B. Investments

PEC continually reviews its investments to determine whether a decline in fair value below the cost basis is other than temporary. In 2003, PEC's affordable housing investment (AHI) portfolio was reviewed and deemed to be impaired based on various factors including continued operating losses of the AHI portfolio and management performance issues arising at certain properties within the AHI portfolio. As a result, PEC recorded an impairment on the AHI portfolio of $18 million on a pre-tax basis during the fourth quarter of 2003. PEC also recorded an impairment of $3 million on a cost investment.

PEC obtained a valuation study to assess its investment in Interpath Communications, Inc. (Interpath) based on current valuations in the technology sector during 2001. Interpath was an application service provider business in which PEC had a 35% ownership interest. As a result of the valuation study, PEC recorded investment impairments for other-than-temporary declines in the fair value of its investment in Interpath. The investment write-down was $157 million on a pre-tax basis for the year ended December 31, 2001. In May 2002, Interpath merged with a third party and PEC's ownership was diluted to approximately 19% of Interpath. As a result, PEC reviewed the Interpath investment for impairment and wrote off the remaining amount of its cost-basis investment in Interpath, recording a pre-tax impairment of $25 million in the third quarter of 2002. In the fourth quarter of 2002, PEC sold its remaining interest in Interpath for a nominal amount.

7. Equity

A. Capitalization

At December 31, 2003, PEC was authorized to issue up to 200 million shares of common stock. All shares issued and outstanding are held by the Company. Preferred stock outstanding at December 31, 2003 and 2002 consisted of the following (in millions except per share and par value):

Authorized – 300,000 shares, cumulative, $100 par value Preferred Stock; 20,000,000 shares, cumulative, $100 par value Serial Preferred Stock	
$5.00 Preferred – 236,997 shares (redemption price $110.00)	$ 24
$4.20 Serial Preferred – 100,000 shares outstanding redemption price $102.00)	10
$5.44 Serial Preferred –249,850 shares (redemption price $101.00)	25
Total Preferred Stock	$ 59

There are various provisions limiting the use of retained earnings for the payment of dividends under certain circumstances. At December 31, 2003, there were no significant restrictions on the use of retained earnings.

PEC's Articles of Incorporation provide that cash dividends on common stock shall be limited to 75% of net income available for dividends if common stock equity falls below 25% of total capitalization, and to 50% if common stock equity falls below 20%. On December 31, 2003, PEC's common stock equity was approximately 50.7% of total capitalization.

Refer to Note 8 for additional dividend restrictions related to PEC's mortgage.

B. Stock-Based Compensation Plans

Employee Stock Ownership Plan

Progress Energy sponsors the Progress Energy 401(k) Savings and Stock Ownership Plan (401(k)) for which substantially all full-time non-bargaining unit employees and certain part-time non-bargaining employees within participating subsidiaries are eligible. PEC is a participating subsidiary of the 401(k), which has matching and incentive goal features, encourages systematic savings by employees and provides a method of acquiring Progress Energy common stock and other diverse investments. The 401(k), as amended in 1989, is an Employee Stock Ownership Plan (ESOP) that can enter into acquisition loans to acquire Progress Energy common stock to satisfy 401(k) common stock needs. Qualification as an ESOP did not change the level of benefits received by employees under the 401(k). Common stock acquired with the proceeds of an ESOP loan is held by the 401(k) Trustee in a suspense account. The common stock is released from the suspense account and made available for allocation to participants as the ESOP loan is repaid. Such allocations are used to partially meet common stock needs related to Progress Energy matching and incentive contributions and/or reinvested dividends.

There were 4.0 million and 4.6 million ESOP suspense shares at December 31, 2003 and 2002, respectively, with a fair value of $183 million and $200 million, respectively. PEC's matching and incentive goal compensation cost under the 401(k) is determined based on matching percentages and incentive goal attainment as defined in the plan. Such compensation cost is allocated to participants' accounts in the form of Progress Energy common stock, with the number of shares determined by dividing compensation cost by the common stock market value at the time of allocation. The 401(k) common stock share needs are met with open market purchases, with shares released from the ESOP suspense account and with newly issued shares. Costs for incentive goal compensation are accrued during the fiscal year and typically paid with shares in the following year; costs for the matching component are typically met with shares in the same year incurred. PEC's matching and incentive cost which were and will be met with shares released from the suspense account totaled approximately $11 million, $13 million and $13 million for the years ended December 31, 2003, 2002 and 2001, respectively. Matching and incentive cost totaled approximately $16 million, $14 million and $14 million for the years ended December 31, 2003, 2002 and 2001, respectively. PEC has a long-term note receivable from the 401(k) Trustee related to the purchase of common stock from PEC in 1989 (now Progress Energy common stock). The balance of the note receivable from the 401(k) Trustee is included in the determination of unearned ESOP common stock, which reduces common stock equity. Interest income on the note receivable is not recognized for financial statement purposes.

Stock Option Agreements

Pursuant to Progress Energy's 1997 Equity Incentive Plan and 2002 Equity Incentive Plan, as amended and restated as of July 10, 2002, Progress Energy may grant options to purchase shares of common stock to directors, officers and eligible employees. For the years ended December 31, 2003, 2002 and 2001, respectively, approximately 3.0 million, 2.9 million and 2.4 million common stock options were granted. Of these amounts, approximately 1.9 million, 1.2 million and 1.0 million options were granted to officers and eligible employees of PEC in 2003, 2002 and 2001, respectively.

Other Stock-Based Compensation Plans

Progress Energy has additional compensation plans for officers and key employees that are stock-based in whole or in part. PEC participates in these plans. The two primary active stock-based compensation programs are the Performance Share Sub-Plan (PSSP) and the Restricted Stock Awards program (RSA), both of which were established pursuant to Progress Energy's 1997 Equity Incentive Plan and were continued under the 2002 Equity Incentive Plan, as amended and restated as of July 10, 2002.

Under the terms of the PSSP, officers and key employees are granted performance shares on an annual basis that vest over a three-year consecutive period. Each performance share has a value that is equal to, and changes with, the value of a share of Progress Energy's common stock, and dividend equivalents are accrued on, and reinvested in, the performance shares. The PSSP has two equally weighted performance measures, both of which are based on Progress Energy's results as compared to a peer group of utilities. Compensation expense is recognized over the vesting period based on the expected ultimate cash payout and is reduced by any forfeitures.

The RSA program allows the Company to grant shares of restricted common stock to officers and key employees of the Company. The restricted shares generally vest on a graded vesting schedule over a minimum of three years. Compensation expense, which is based on the fair value of common stock at the grant date, is recognized over the applicable vesting period and is reduced by any forfeitures.

The total amount expensed by PEC for other stock-based compensation plans was $15 million, $11 million and $10 million in 2003, 2002 and 2001, respectively.

C. Accumulated Other Comprehensive Loss

Components of accumulated other comprehensive loss are as follows:

(in millions)	**2003**	2002
Loss on cash flow hedges	**$ (6)**	$ (10)
Minimum pension liability adjustments	**(1)**	(73)
Total accumulated other comprehensive loss	**$ (7)**	$ (83)

7. Debt and Credit Facilities

A. Debt and Credit

At December 31, PEC's long-term debt consisted of the following (maturities and weighted-average interest rates at December 31, 2003):

(in millions)		**2003**	2002
First mortgage bonds, maturing 2004-2033	6.42%	**$ 1,900**	$ 1,550
Pollution control obligations, maturing 2010-2024	1.69%	**708**	708
Unsecured notes, maturing 2012	6.50%	**500**	500
Medium-term notes, maturing 2008	6.65%	**300**	300
Miscellaneous notes		**-**	6
Unamortized premium and discount, net		**(22)**	(16)
Current portion of long-term debt		**(300)**	-
Total Long-Term Debt, Net		**$ 3,086**	$ 3,048

At December 31, 2003, PEC had committed lines of credit, which are used to support its commercial paper borrowings and had no outstanding loans. PEC is required to pay minimal annual commitment fees to maintain its credit facilities. The following table summarizes PEC's credit facilities (in millions):

Description	Total
364-Day (expiring 7/29/04)	$ 165
3-Year (expiring 7/31/05)	285
	$ 450

At December 31, 2003 and 2002, PEC had $4 million and $438 million, respectively, of outstanding commercial paper and other short term debt classified as short term obligations. The weighted-average interest rates of such short-term obligations at December 31, 2003 and 2002 were 2.25% and 1.74%, respectively.

The combined aggregate maturities of long-term debt for 2004 through 2008 are approximately, in millions, $300, $300, $0, $200 and $300, respectively.

B. Covenants and Default Provisions

Financial Covenants
PEC's credit line contains various terms and conditions that could affect PEC's ability to borrow under these facilities. These include a maximum debt to total capital ratio, a material adverse change clause and a cross-default provision.

PEC's credit line requires a maximum total debt to total capital ratio of 65%. Indebtedness as defined by the bank agreement includes certain letters of credit and guarantees which are not recorded on the Consolidated Balance Sheets. At December 31, 2003, PEC's total debt to total capital ratio was 51.4%.

Material Adverse Change Clause
The credit facility of PEC includes a provision under which lenders could refuse to advance funds in the event of a material adverse change in the borrower's financial condition.

Default Provisions
PEC's credit lines include cross-default provisions for defaults of indebtedness in excess of $10 million. PEC's cross-default provisions only apply to defaults of indebtedness by PEC and its subsidiaries, respectively, and not to other affiliates of PEC. In addition, the credit lines of Progress Energy include a similar provision. Progress Energy's cross-default provisions only apply to defaults of indebtedness by Progress Energy and its significant subsidiaries, which includes PEC.

The lenders may accelerate payment of any outstanding debt if cross-default provisions are triggered. Any such acceleration would cause a material adverse change in the respective company's financial condition. Certain agreements underlying PEC's indebtedness also limit PEC's ability to incur additional liens or engage in certain types of sale and leaseback transactions.

Other Restrictions
PEC's mortgage indenture provides that, as long as any first mortgage bonds are outstanding, cash dividends and distributions on PEC's common stock and purchases of PEC's common stock are restricted to aggregate net income available for PEC, since December 31, 1948, plus $3 million, less the amount of all preferred stock dividends and distributions, and all common stock purchases, since December 31, 1948. At December 31, 2003, none of PEC's retained earnings were restricted. Refer to Note 7 for additional dividend restrictions related to PEC's Articles of Incorporation.

C. Secured Obligations

PEC's first mortgage bonds are secured by their respective mortgage indentures. PEC's mortgage constitutes a first lien on substantially all of its fixed properties, subject to certain permitted encumbrances and exceptions. The PEC mortgage also constitutes a lien on subsequently acquired property. At December 31, 2003, PEC had approximately $2,608 million in first mortgage bonds outstanding including those related to pollution control obligations. The PEC mortgage allows the issuance of additional mortgage bonds upon the satisfaction of certain conditions.

D. Hedging Activities

PEC uses interest rate derivatives to adjust the fixed and variable rate components of its debt portfolio and to hedge cash flow risk of fixed rate debt to be issued in the future. See discussion of risk management and derivative transactions at Note 12.

9. Fair Value of Financial Instruments

At December 31, 2003 and 2002, there were miscellaneous investments consisting primarily of investments in company-owned life insurance and other benefit plan assets with carrying amounts totaling approximately $59 million and $54 million, respectively, included in miscellaneous other property and investments. The carrying amount of these investments approximates fair value due to the short maturity of certain instruments. Other instruments are presented at fair value in accordance with GAAP. The carrying amount of PEC's long-term debt, including current maturities, was $3,386 million at December 31, 2003 and $3,048 million at December 31, 2002. The estimated fair value of this debt, as obtained from quoted market prices for the same or similar issues, was $3,686 million and $3,328 million at December 31, 2003 and 2002, respectively.

External trust funds have been established to fund certain costs of nuclear decommissioning. These nuclear decommissioning trust funds are invested in stocks, bonds and cash equivalents. Nuclear decommissioning trust funds are presented at amounts that approximate fair value. Fair value is obtained from quoted market prices for the same or similar investments.

10. Income Taxes

Deferred income taxes are provided for temporary differences between book and tax bases of assets and liabilities. Investment tax credits related to regulated operations are amortized over the service life of the related property. To the extent that the establishment of deferred income taxes under SFAS No. 109 is different from the recovery of taxes by PEC through the ratemaking process, the differences are deferred pursuant to SFAS No. 71. A regulatory asset or liability has been recognized for the impact of tax expenses or benefits that are recovered or refunded in different periods by the utilities pursuant to rate orders.

Net accumulated deferred income tax liabilities/(assets) at December 31 are:

(in millions)	**2003**	2002
Accumulated depreciation and property cost differences	**$ 1,207**	$ 1,280
Minimum pension liability	**(1)**	(47)
Deferred costs, net	**(26)**	(50)
Income tax credit carry forward	**(22)**	(10)
Valuation allowance	**1**	8
Miscellaneous other temporary differences, net	**(50)**	(10)
Net accumulated deferred income tax liability	**$ 1,109**	$ 1,171

Total deferred income tax liabilities were $1,880 million and $1,882 million at December 31, 2003 and 2002, respectively. Total deferred income tax assets were $771 million and $711 million at December 31, 2003 and 2002, respectively. At December 31, 2003 and 2002, PEC had net non-current deferred tax liabilities of $1,125 million and $1,105 million. At December 31, 2003 PEC had a net current deferred tax asset of $16 million which is included on the Consolidated Balance Sheets under the caption prepayments and other current assets. At December 31, 2002 PEC had a net current deferred tax liability of $66 million which is included on the Consolidated Balance Sheets under the caption other current liabilities.

PEC established additional valuation allowances of $1 million, $4 million and $4 million during 2003, 2002 and 2001, respectively, due to the uncertainty of realizing certain future state tax benefits. PEC had a valuation allowance of $8 million at December 31, 2002, which decreased by $7 million in 2003. The overall decrease in the 2003 valuation allowance is largely due to PEC's sale of its wholly-owned subsidiary Caronet. Caronet's valuation allowance balance at December 31, 2002 and 2001 was $8 million and $4 million, respectively. PEC believes that it is more likely than not that the results of future operations will generate sufficient taxable income to allow for the utilization of the remaining deferred tax assets.

Reconciliations of PEC's effective income tax rate to the statutory federal income tax rate are:

	2003	2002	2001
Effective income tax rate	**32.6%**	32.5%	38.0%
State income taxes, net of federal benefit	**(1.9)**	(3.1)	(3.2)
Investment tax credit amortization	**1.4**	1.9	2.5
Progress Energy tax benefit allocation	**3.0**	5.0	-
Other differences, net	**(0.1)**	(1.3)	(2.3)
Statutory federal income tax rate	**35.0%**	35.0%	35.0%

The provisions for income tax expense are comprised of:

(in millions)	**2003**	2002	2001
Income tax expense (credit):			
Current - federal	**$ 285**	$ 265	$ 349
state	**37**	36	39
Deferred - federal	**(55)**	(76)	(140)
state	**(13)**	(6)	(10)
Investment tax credit	**(10)**	(12)	(15)
Total income tax expense	**$ 244**	$ 207	$ 223

PEC and each of its wholly-owned subsidiaries have entered into a Tax Agreement with Progress Energy (See Note 1C). PEC's intercompany tax receivable was $16 million and $13 million at December 31, 2003 and 2002, respectively.

11. Benefit Plans

PEC and some of its subsidiaries have a non-contributory defined benefit retirement (pension) plan for substantially all full-time employees. PEC also has supplementary defined benefit pension plans that provide benefits to higher-level employees. In addition to pension benefits, PEC and some of its subsidiaries provide contributory other postretirement benefits (OPEB), including certain health care and life insurance benefits, for retired employees who meet specified criteria. PEC uses a measurement date of December 31 for its pension and OPEB plans.

The components of net periodic benefit cost for the years ended December 31 are:

	Pension Benefits			Other Postretirement Benefits		
(in millions)	**2003**	2002	2001	**2003**	2002	2001
Service cost	**$ 23**	$ 19	$ 17	**$ 7**	$ 6	$ 7
Interest cost	**51**	51	47	**15**	14	14
Expected return on plan assets	**(70)**	(73)	(72)	**(3)**	(3)	(4)
Amortization, net	**-**	1	(6)	**5**	2	5
Net periodic cost / (benefit)	**$ 4**	$ (2)	$ (14)	**$ 24**	$ 19	$ 22

Prior service costs and benefits are amortized on a straight-line basis over the average remaining service period of active participants. Actuarial gains and losses in excess of 10% of the greater of the obligation or the market-related value of assets are amortized over the average remaining service period of active participants. PEC uses a five-year averaging method to determine its market-related value of assets.

Reconciliations of the changes in the plans' benefit obligations and the plans' funded status are:

	Pension Benefits		Other Postretirement Benefits	
(in millions)	**2003**	2002	**2003**	2002
Obligation at January 1	**$ 802**	$ 682	**$ 234**	$ 192
Service cost	**23**	19	**7**	6
Interest cost	**51**	51	**15**	14
Benefit payments	**(46)**	(46)	**(8)**	(9)
Actuarial loss (gain)	**(82)**	96	**12**	31
Obligation at December 31	**748**	802	**260**	234
Fair value of plan assets at December 31	**694**	574	**43**	33
Funded status	**(54)**	(228)	**(217)**	(201)
Unrecognized transition obligation	**-**	-	**23**	26
Unrecognized prior service cost	**4**	4	**-**	-
Unrecognized net actuarial (gain) loss	**61**	238	**41**	38
Minimum pension liability adjustment	**(2)**	(125)	**-**	-
Prepaid (accrued) cost at December 31, net	**$ 9**	$ (111)	**$ (153)**	$ (137)

The net prepaid pension cost of $9 million at December 31, 2003 is recognized in the accompanying Consolidated Balance Sheets as prepaid pension cost of $28 million, which is included in other assets and deferred debits, and accrued benefit cost of $19 million, which is included in other liabilities and deferred credits. The accrued pension cost at December 31, 2002 is included in other liabilities and deferred credits in the accompanying Consolidated Balance Sheets. The defined benefit pension plans with accumulated benefit obligations in excess of plan assets had projected benefit obligations totaling $22 million and $802 million at December 31, 2003 and 2002, respectively. Those plans had accumulated benefit obligations totaling $19 million and $685 million, respectively, no plan assets at December 31, 2003, and plan assets totaling $574 million at December 31, 2002. The total accumulated benefit obligation for pension plans was $745 million and $685 million at December 31, 2003 and 2002, respectively. The accrued OPEB cost is included in other liabilities and deferred credits in the accompanying Consolidated Balance Sheets.

A minimum pension liability adjustment of $2 million, related to the supplementary defined benefit pension plan, was recorded at December 31, 2003. This adjustment is offset by a corresponding pre-tax amount in accumulated other comprehensive loss, a component of common stock equity. Due to a combination of decreases in the fair value of plan assets and a decrease in the discount rate used to measure the pension obligation, a minimum pension liability adjustment of $125 million was recorded at December 31, 2002. This adjustment resulted in a charge of $4 million to intangible assets, included in other assets and deferred debits in the accompanying Consolidated Balance Sheets, and a pre-tax charge of $121 million to accumulated other comprehensive loss, a component of common stock equity.

Reconciliations of the fair value of plan assets are:

	Pension Benefits		Other Postretirement Benefits	
(in millions)	**2003**	2002	**2003**	2002
Fair value of plan assets January 1	**$ 574**	$ 717	**$ 33**	$ 38
Actual return on plan assets	**164**	(97)	**10**	(5)
Benefit payments	**(46)**	(46)	**(8)**	(9)
Employer contributions	**1**	1	**8**	9
Transfers	**-**	(1)	**-**	-
Fair value of plan assets at December 31	**$ 693**	$ 574	**$ 43**	$ 33

In the table above, substantially all employer contributions represent benefit payments made directly from Company assets. The remaining benefits payments were made directly from plan assets. The OPEB benefit payments represent the net PEC cost after participant contributions. Participant contributions represent approximately 35% of gross benefit payments.

The asset allocation for PEC's plans at the end of 2003 and 2002 and the target allocation for the plans, by asset category, are as follows:

	Pension Benefits			Other Postretirement Benefits		
	Target Allocations	Percentage of Plan Assets at Year End		Target Allocations	Percentage of Plan Assets at Year End	
Asset Category	2004	**2003**	2002	2004	**2003**	2002
Equity – domestic	50%	**49%**	47%	50%	**49%**	47%
Equity – international	15%	**22%**	20%	15%	**22%**	20%
Debt – domestic	15%	**11%**	15%	15%	**11%**	15%
Debt – international	10%	**11%**	10%	10%	**11%**	10%
Other	10%	**7%**	8%	10%	**7%**	8%
Total	100%	**100%**	100%	100%	**100%**	100%

PEC sets target allocations among asset classes to provide broad diversification to protect against large investment losses and excessive volatility, while recognizing the importance of offsetting the impacts of benefit cost escalation. In addition, PEC employs external investment managers who have complementary investment philosophies and approaches. Tactical shifts (plus or minus five percent) in asset allocation from the target allocations are made based on the near-term view of the risk and return tradeoffs of the asset classes.

In 2004, PEC expects to make required contributions of $17 million directly to pension plan assets. The expected benefit payments for the pension benefit plan for 2004 through 2008 and in total for 2009-2013, in millions, are approximately $48, $49, $50, $53, $55 and $301, respectively. The expected benefit payments for the OPEB plan for 2004 through 2008 and in total for 2009-2013, in millions, are approximately $7, $8, $9, $10, $10 and $62, respectively. The expected benefit payments include benefit payments directly from plan assets and benefit payments directly from Company assets. The benefit payment amounts reflect the net cost to PEC after any participant contributions.

The following weighted-average actuarial assumptions were used in the calculation of the year-end obligation:

	Pension Benefits		Other Postretirement Benefits	
	2003	2002	**2003**	2002
Discount rate	**6.30%**	6.60%	**6.30%**	6.60%
Rate of increase in future compensation – non-bargaining	-	4.00%	-	-
Rate of increase in future compensation – supplementary plan	**5.00%**	4.00%	-	-
Initial medical cost trend rate for pre-Medicare benefits	-	-	**7.25%**	7.50%
Initial medical cost trend rate for post-Medicare benefits	-	-	**7.25%**	7.50%
Ultimate medical cost trend rate	-	-	**5.25%**	5.25%
Year ultimate medical cost trend rate is achieved	-	-	**2009**	2009

PEC's primary defined benefit retirement plan for non-bargaining employees is a "cash balance" pension plan as defined in EITF Issue No. 03-4. Therefore, effective December 31, 2003, PEC began to use the traditional unit credit method for purposes of measuring the benefit obligation of this plan and will use that method to measure future benefit costs. Under the traditional unit credit method, no assumptions are included about future changes in compensation and the accumulated benefit obligation and projected benefit obligation are the same.

The following weighted-average actuarial assumptions were used in the calculation of the net periodic cost:

	Pension Benefits			Other Postretirement Benefits		
	2003	2002	2001	**2003**	2002	2001
Discount rate	**6.60%**	7.50%	7.50%	**6.60%**	7.50%	7.50%
Rate of increase in future compensation	**4.00%**	4.00%	4.00%	-	-	-
Expected long-term rate of return on plan assets	**9.25%**	9.25%	9.25%	**9.25%**	9.25%	9.25%
Initial medical cost trend rate for pre-Medicare benefits	-	-	-	**7.50%**	7.50%	7.50%
Initial medical cost trend rate for post-Medicare benefits	-	-	-	**7.50%**	7.50%	7.50%
Ultimate medical cost trend rate	-	-	-	**5.25%**	5.00%	5.00%
Year ultimate medical cost trend rate is achieved	-	-	-	**2009**	2008	2007

The expected long-term rates of return on plan assets were determined by considering long-term historical returns for the plans and long-term projected returns based on the plans' target asset allocations. Those benchmarks support an expected long-term rate of return between 9.5% and 10.0%. PEC has chosen to use an expected long-term rate of 9.25% due to the uncertainties of future returns.

The medical cost trend rates were assumed to decrease gradually from the initial rates to the ultimate rates. Assuming a 1% increase in the medical cost trend rates, the aggregate of the service and interest cost components of the net periodic OPEB cost for 2003 would increase by $1 million, and the OPEB obligation at December 31, 2003, would increase by $18 million. Assuming a 1% decrease in the medical cost trend rates, the aggregate of the service and interest cost components of the net periodic OPEB cost for 2003 would decrease by $1 million and the OPEB obligation at December 31, 2003, would decrease by $15 million.

In December 2003, the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Act) was signed into law. In accordance with guidance issued by the FASB in FASB Staff Position FAS 106-1, PEC has elected to defer accounting for the effects of the Act due to uncertainties regarding the effects of the implementation of the Act and the accounting for certain provisions of the Act. Therefore, OPEB information presented above and in the financial statements does not reflect the effects of the Act. When specific authoritative accounting guidance is issued, it could require plan sponsors to change previously reported information. PEC is in the early stages of reviewing the Act and determining its potential effects on PEC.

12. Risk Management Activities and Derivatives Transactions

Under its risk management policy, PEC may use a variety of instruments, including swaps, options and forward contracts, to manage exposure to fluctuations in commodity prices and interest rates. Such instruments contain credit risk if the counterparty fails to perform under the contract. PEC minimizes such risk by performing credit reviews using, among other things, publicly available credit ratings of such counterparties. Potential non-performance by counterparties is not expected to have a material effect on the consolidated financial position or consolidated results of operations of PEC.

A. Commodity Contracts – General

Most of PEC's commodity contracts either are not derivatives pursuant to SFAS No. 133 or qualify as normal purchases or sales pursuant to SFAS No. 133. Therefore, such contracts are not recorded at fair value.

In connection with the January 2003 EITF meeting, the FASB was requested to reconsider an interpretation of SFAS No. 133. The interpretation, which was contained in the Derivative Implementation Group's C11 guidance, related to the pricing of contracts that include broad market indices (e.g., CPI). In particular, that guidance discussed whether the pricing in a contract that contains broad market indices could qualify as a normal purchase or sale (the normal purchase or sale term is a defined accounting term, and may not, in all cases, indicate whether the contract would be "normal" from an operating entity viewpoint). In June 2003, the FASB issued final superseding guidance (DIG Issue C20) on this issue. The new guidance was effective October 1, 2003 for the Company. DIG Issue C20 specifies new pricing-related criteria for qualifying as a normal purchase or sale, and it required a special transition adjustment as of October 1, 2003.

PEC determined that it had one existing "normal" contract that was affected by DIG Issue C20. Pursuant to the provisions of DIG Issue C20, PEC recorded a pre-tax fair value loss transition adjustment of $38 million ($23 million after-tax) in the fourth quarter of 2003, which was recorded as a cumulative effect of a change in accounting principle. The subject contract meets the DIG Issue C20 criteria for normal purchase or sale and, therefore, was designated as a normal purchase as of October 1, 2003. The liability associated with the fair value loss will be amortized to earnings over the term of the related contract.

B. Commodity Derivatives – Economic Hedges and Trading

Nonhedging derivatives, primarily electricity forward contracts, are entered into for trading purposes and for economic hedging purposes. While management believes the economic hedges mitigate exposures to fluctuations in commodity prices, these instruments are not designated as hedges for accounting purposes and are monitored consistent with trading positions. PEC manages open positions with strict policies that limit its exposure to market risk and require daily reporting to management of potential financial exposures. Gains and losses from such contracts were not material during 2003, 2002 or 2001, and PEC did not have material outstanding positions in such contracts at December 31, 2003 or 2002.

C. Interest Rate Derivatives – Fair Value or Cash Flow Hedges

PEC manages its interest rate exposure in part by maintaining its variable-rate and fixed-rate exposures within defined limits. In addition, PEC also enters into financial derivative instruments including, but not limited to, interest rate swaps and lock agreements to manage and mitigate interest rate risk exposure.

PEC uses cash flow hedging strategies to hedge variable interest rates on long-term debt and to hedge interest rates with regard to future fixed-rate debt issuances. PEC held no interest rate cash flow hedges at December 31, 2003 or 2002. At December 31, 2003, $1 million of net after-tax deferred losses in accumulated other comprehensive income, related to terminated hedges, will be reclassified to earnings during the next 12 months as the hedged interest payments occur.

PEC uses fair value hedging strategies to manage its exposure to fixed interest rates on long-term debt. At December 31, 2003 and 2002, PEC had no open interest rate fair value hedges.

The notional amounts of interest rate derivatives are not exchanged and do not represent exposure to credit loss. In the event of default by a counterparty, the risk in these transactions is the cost of replacing the agreements at current market rates.

13. Related Party Transactions

PEC participates in an internal money pool, operated by Progress Energy, to more effectively utilize cash resources and to reduce outside short-term borrowings. The money pool also is used to settle intercompany balances. The weighted-average interest rate for the money pool was 1.47%, 2.18% and 4.47% at December 31, 2003, 2002 and 2001, respectively. At December 31, 2003, PEC had $25 million of amounts payable to the money pool that are included in notes payable to affiliated companies on the Consolidated Balance Sheets. At December 31, 2002, PEC had $50 million of amounts receivable from the money pool that are included in notes receivable from affiliated companies on the Consolidated Balance Sheets. PEC recorded net interest expense of approximately $1 million related to the money pool for 2003 and 2002. Net interest expense for 2001 was not significant.

The Company formed Progress Energy Service Company, LLC (PESC) to provide specialized services, at cost, to the Company and its subsidiaries, as approved by the U.S. Securities and Exchange Commission (SEC). PEC has an agreement with PESC under which services, including purchasing, information technology, telecommunications, marketing, treasury, human resources, accounting, real estate, legal and tax are rendered at cost. Amounts billed to PEC by PESC for these services during 2003, 2002 and 2001 amounted to $184 million, $198 million and $156 million, respectively. At December 31, 2003 and 2002, PEC had net payables of $118 million and $63 million, respectively, to PESC. During 2002, the Office of Public Utility Regulation within the SEC completed an audit examination of the Company's books and records. This examination is a standard process for all PUHCA registrants. Based on the review, the method for allocating PESC costs to the Company and its affiliates changed for 2003 and retroactive reallocations of 2002 and 2001 charges were made during the first quarter. The net after-tax impact of the reallocation of costs was a reduction of expenses at PEC by $10 million.

The Company sold North Carolina Natural Gas Corporation (NCNG) to Piedmont Natural Gas Company, Inc. on September 30, 2003. During the years ended December 31, 2003, 2002 and 2001, gas sales from NCNG to PEC amounted to $11 million, $18 million and $15 million, respectively. The gas sales for 2003 indicated above exclude any sales subsequent to September 2003.

PEC entered into a Tax Agreement with Progress Energy (See Note 10).

In February 2002, PEC transferred the Rowan Plant to Progress Ventures, Inc. The property and inventory transferred totaled approximately $244 million.

In August 2002, PEC transferred reservation payments for the manufacture of two combustion turbines to PEF at PEC's original cost of $20 million.

14. Financial Information by Business Segment

PEC's operations consist primarily of the PEC Electric segment which is engaged in the generation, transmission, distribution and sale of electric energy primarily in portions of North Carolina and South Carolina. These electric operations are subject to the rules and regulations of the FERC, the NCUC, the SCPSC and the NRC.

The Other segment, whose operations are primarily in the United States, is made up of other nonregulated business areas including telecommunications and other nonregulated subsidiaries that do not separately meet the disclosure requirements of SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information" and consolidation entities and eliminations. Included are the operations of Caronet, which recognized an $87 million after-tax asset and investment impairment in 2002 and an after-tax investment impairment of $107 million in 2001.

(In millions)	PEC Electric	Other	Total
Year Ended December 31, 2003			
Revenues	**$ 3,589**	**$ 11**	**$ 3,600**
Depreciation and amortization	**562**	**1**	**563**
Total interest charges, net	**194**	**-**	**194**
Impairment of long-lived assets & investments	**11**	**10**	**21**
Income taxes	**240**	**4**	**244**
Income before cumulative effect	**515**	**(13)**	**502**
Total segment assets	**10,854**	**154**	**11,008**
Capital and investment expenditures	**470**	**1**	**471**
Year Ended December 31, 2002			
Revenues	$ 3,539	$ 15	$ 3,554
Depreciation and amortization	524	4	528
Total interest charges, net	212	-	212
Impairment of long-lived assets & investments	-	126	126
Income taxes	237	(30)	207
Income before cumulative effect	513	(85)	428
Total segment assets	10,139	266	10,405
Capital and investment expenditures	624	12	636
Year Ended December 31, 2001			
Revenues	$ 3,344	$ 16	$ 3,360
Depreciation and amortization	522	7	529
Total interest charges, net	241	-	241
Impairment of long-lived assets & investments	-	157	157
Income taxes	264	(41)	223
Income before cumulative effect	468	(107)	361
Capital and investment expenditures	824	13	837

15. Other Income and Other Expense

Other income and expense includes interest income, gain on the sale of investments, impairment of investments and other income and expense items as discussed below. The components of other, net as shown on the Consolidated Statements of Income and Comprehensive Income for years ended December 31, are as follows:

(in millions)	**2003**	2002	2001
Other income			
Net financial trading gain (loss)	**$ (1)**	$ (2)	$ 3
Net energy brokered for resale gain	**2**	1	3
Nonregulated energy and delivery services income	**8**	12	12
Investment gains	**9**	22	2
AFUDC equity	**2**	6	9
Other	**12**	21	13
Total other income	**$ 32**	$ 60	$ 42
Other expense			
Nonregulated energy and delivery services expenses	**$ 9**	$ 14	$ 21
Donations	**6**	8	11
Investment losses	**12**	14	4
Other	**16**	11	10
Total other expense	**$ 43**	$ 47	$ 46
Other, net	**$ (11)**	$ 13	$ (4)

Net financial trading gain (loss) represents non-asset-backed trades of electricity and gas. Nonregulated energy and delivery services include power protection services and mass market programs (surge protection, appliance services and area light sales) and delivery, transmission and substation work for other utilities.

16. Commitments and Contingencies

A. Purchase Obligations

The following table reflects PEC's contractual cash obligations and other commercial commitments in the respective periods in which they are due.

(in millions) Contractual Cash Obligations	2004	2005	2006	2007	2008	Thereafter
Fuel	$ 433	$ 244	$ 195	$ 96	$ 33	$ 73
Purchased power	110	110	110	110	74	474
Construction Obligations	5	-	-	-	-	-
Other Purchase Obligations	-	-	-	-	-	13
Total	$ 548	$ 354	$ 305	$ 206	$ 107	$ 560

Fuel and Purchased Power

PEC has entered into various long-term contracts for coal, gas and oil requirements of its generating plants. Total payments under these commitments were $498 million, $529 million and $496 million in 2003, 2002 and 2001, respectively. Estimated annual payments for firm commitments of fuel purchases and transportation costs under these contracts are approximately $433 million, $244 million, $195 million, $96 million and $33 million for 2004 through 2008, respectively, with $73 million payable thereafter.

Pursuant to the terms of the 1981 Power Coordination Agreement, as amended, between PEC and the North Carolina Eastern Municipal Power Agency (Power Agency), PEC is obligated to purchase a percentage of Power Agency's ownership capacity of, and energy from, the Harris Plant. In 1993, PEC and Power Agency entered into an agreement to restructure portions of their contracts covering power supplies and interests in jointly owned units. Under the terms of the 1993 agreement, PEC increased the amount of capacity and energy purchased from Power Agency's ownership interest in the Harris Plant, and the buyback period was extended six years through 2007. The estimated minimum annual payments for these purchases, which reflect capacity costs, total approximately $36 million. These contractual purchases totaled $36 million, $36 million and $33 million for 2003, 2002 and 2001, respectively. In 1987, the NCUC ordered PEC to reflect the recovery of the capacity portion of these costs on a levelized basis over the original 15-year buyback period, thereby deferring for future recovery the difference between such costs and amounts collected through rates. In 1988, the SCPSC ordered similar treatment, but with a 10-year levelization period. At December 31, 2002, PEC had deferred purchased capacity costs, including carrying costs accrued on the deferred balances of $17 million. At December 31, 2003 all previously deferred costs have been expensed.

PEC has a long-term agreement for the purchase of power and related transmission services from Indiana Michigan Power Company's Rockport Unit No. 2 (Rockport). The agreement provides for the purchase of 250 MW of capacity through 2009 with estimated minimum annual payments of approximately $42 million, representing capital-related capacity costs. Estimated annual payments for energy and capacity costs are approximately $70 million through 2009. Total purchases (including energy and transmission use charges) under the Rockport agreement amounted to $66 million, $59 million and $63 million for 2003, 2002 and 2001, respectively.

Effective June 1, 2001, PEC executed a long-term agreement for the purchase of power from Skygen Energy LLC's Broad River facility (Broad River). The agreement provides for the purchase of approximately 500 MW of capacity through 2021 with an original minimum annual payment of approximately $16 million, primarily representing capital-related capacity costs. A separate long-term agreement for additional power from Broad River commenced June 1, 2002. This agreement provided for the additional purchase of approximately 300 MW of capacity through 2022 with an original minimum annual payment of approximately $16 million representing capital-related capacity costs. Total purchases under the Broad River agreements amounted to $37 million, $38 million, and $21 million in 2003, 2002 and 2001 respectively.

PEC has various pay-for-performance purchased power contracts with certain cogenerators (qualifying facilities) for approximately 400 MW of capacity expiring at various times through 2009. These purchased power contracts generally provide for capacity and energy payments. Payments for both capacity and energy are contingent upon the QFs' ability to generate. Payments made under these contracts were $118 million in 2003 and $145 million in 2002 and 2001.

Construction Obligations

PEC has purchase obligations for various combustion turbines. Total purchases under these obligations were $21 million for 2003 and $13 million for 2002. Future purchase obligations are $5 million for 2004.

Other Contractual Obligations

On December 31, 2002, PEC entered into a contractual commitment to purchase at least $13 million of capital parts by December 31, 2010. At December 31, 2003 no capital parts have been purchased under this contract.

B. Leases

PEC leases office buildings, computer equipment, vehicles, and other property and equipment with various terms and expiration dates. Rent expense under operating leases totaled $11 million, $10 million and $22 million for 2003, 2002 and 2001, respectively. Assets recorded under capital leases consist of:

(in millions)	**2003**	2002
Buildings	**$ 30**	$ 28
Less: Accumulated amortization	**(10)**	(10)
	$ 20	$ 18

Minimum annual rental payments, excluding executory costs such as property taxes, insurance and maintenance, under long-term noncancelable leases at December 31, 2003 are:

(in millions)	Capital Leases	Operating Leases
2004	$ 2	$ 6
2005	2	9
2006	2	6
2007	2	6
2008	2	6
Thereafter	25	102
	$ 35	$ 135
Less amount representing imputed interest	(15)	
Present value of net minimum lease payments	$ 20	

PEC is the lessor of electric poles, streetlights and other facilities. Rents received are contingent upon usage and totaled $31 million, $28 million and $31 million for 2003, 2002 and 2001, respectively.

C. Guarantees

As a part of normal business, PEC enters into various agreements providing financial or performance assessments to third parties. Such agreements include, for example, guarantees, standby letters of credit and surety bonds. These agreements are entered into primarily to support or enhance the creditworthiness otherwise attributed to subsidiaries on a stand-alone basis, thereby facilitating the extension of sufficient credit to accomplish the subsidiaries' intended commercial purposes. At December 31, 2003, management does not believe conditions are likely for performance under these agreements.

At December 31, 2003, outstanding guarantees consisted of the following:

(in millions)	
Standby letters of credit	$ 3
Surety bonds	19
Total	$ 22

Standby Letters of Credit
PEC has issued standby letters of credit to financial institutions for the benefit of third parties that have extended credit to PEC and certain subsidiaries. These letters of credit have been issued primarily for the purpose of supporting payments of trade payables, securing performance under contracts and on interest payments on outstanding debt obligations. If a subsidiary does not pay amounts when due under a covered contract, the counterparty may present its claim for payment to the financial institution, which will in turn request payment from PEC. Any amounts owed by its subsidiaries are reflected in the Consolidated Balance Sheets.

Surety Bonds
At December 31, 2003, PEC had $19 million in surety bonds purchased primarily for purposes such as providing workers' compensation coverage and obtaining licenses, permits and rights-of-way. To the extent liabilities are incurred as a result of the activities covered by the surety bonds, such liabilities are included in the Consolidated Balance Sheets.

Guarantees Issued by the Parent
In 2003, PEC determined that its external funding levels did not fully meet the nuclear decommissioning financial assurance levels required by the NRC. Therefore, PEC obtained parent company guarantees of $276 million to meet the required levels.

D. Claims and Uncertainties

1. PEC is subject to federal, state and local regulations addressing hazardous and solid waste management, air and water quality and other environmental matters.

Hazardous and Solid Waste Management

Various organic materials associated with the production of manufactured gas, generally referred to as coal tar, are regulated under federal and state laws. The principal regulatory agency that is responsible for a specific former manufactured gas plant (MGP) site depends largely upon the state in which the site is located. There are several MGP sites to which PEC has some connection. In this regard, PEC and other potentially responsible parties (PRPs) are participating in, investigating and, if necessary, remediating former MGP sites with several regulatory agencies, including, but not limited to, the U.S. Environmental Protection Agency (EPA) and the North Carolina Department of Environment and Natural Resources, Division of Waste Management (DWM). In addition, PEC is periodically notified by regulators such as the EPA and various state agencies of its involvement or potential involvement in sites, other than MGP sites, that may require investigation and/or remediation.

There are nine former MGP sites and other sites associated with PEC that have required or are anticipated to require investigation and/or remediation costs. PEC received insurance proceeds to address costs associated with PEC environmental liabilities related to its involvement with some MGP sites. All eligible expenses related to these are charged against a specific fund containing these proceeds. At December 31, 2003, approximately $9 million remains in this centralized fund with a related accrual of $9 million recorded for the associated expenses of environmental issues. PEC does not believe that it can provide an estimate of the reasonably possible total remediation costs beyond what is currently accrued due to the fact that investigations have not been completed at all sites. PEC measures its liability for these sites based on available evidence including its experience in investigating and remediating environmentally impaired sites. The process often involves assessing and developing cost-sharing arrangements with other PRPs. PEC will accrue costs for the sites to the extent its liability is probable and the costs can be reasonably estimated. Presently, PEC cannot determine the total costs that may be incurred in connection with the remediation of any of these MGP sites.

In September 2003, the Company sold NCNG to Piedmont Natural Gas Company, Inc. As part of the sales agreement, the Company retained responsibility to remediate five former NCNG MGP sites, all of which also are associated with PEC, to state standards pursuant to an Administrative Order by consent. These sites are anticipated to have investigation or remediation costs associated with them. NCNG had previously accrued approximately $2 million for probable and reasonably estimable remediation costs at these sites. These accruals have been recorded on an undiscounted basis. At the time of the sale, the liability for these costs and the related accrual was transferred to PEC. PEC does not believe it can provide an estimate of the reasonably possible total remediation costs beyond the accrual because investigations have not been completed at all sites. Therefore, PEC cannot currently determine the total costs that may be incurred in connection with the investigation and/or remediation of all sites.

PEC has filed claims with its general liability insurance carriers to recover costs arising out of actual or potential environmental liabilities. All claims have settled other than with insolvent carriers. These settlements have not had a material effect on the consolidated financial position or results of operations.

PEC is also currently in the process of assessing potential costs and exposures at other environmentally impaired sites. As the assessments are developed and analyzed, PEC will accrue costs for the sites to the extent the costs are probable and can be reasonably estimated.

Air Quality

There has been and may be further proposed federal legislation requiring reductions in air emissions for NOx, SO2, carbon dioxide and mercury. Some of these proposals establish nation-wide caps and emission rates over an extended period of time. This national multi-pollutant approach to air pollution control could involve significant capital costs which could be material to PEC's consolidated financial position or results of operations. Some companies may seek recovery of the related cost through rate adjustments or similar mechanisms. Control equipment that will be installed on North Carolina fossil generating facilities as part of the North Carolina legislation discussed below may address some of the issues outlined above. However, PEC cannot predict the outcome of this matter.

The EPA is conducting an enforcement initiative related to a number of coal-fired utility power plants in an effort to determine whether modifications at those facilities were subject to New Source Review requirements or New Source Performance Standards under the Clean Air Act. PEC was asked to provide information to the EPA as part of this initiative and cooperated in providing the requested information. The EPA initiated civil enforcement actions against other unaffiliated utilities as part of this initiative. Some of these actions resulted in settlement agreements calling for expenditures by these unaffiliated utilities, ranging from $1.0 billion to $1.4 billion. A utility that was not subject to a civil enforcement action settled its New Source Review issues with the EPA for $300 million. These settlement agreements have generally called for expenditures to be made over extended time periods, and some of the companies may seek recovery of the related cost through rate adjustments or similar mechanisms. PEC cannot predict the outcome of this matter.

In 1998, the EPA published a final rule at Section 110 of the Clean Air Act addressing the regional transport of ozone (NOx SIP Call). The EPA's rule requires 23 jurisdictions, including North Carolina, South Carolina and Georgia, to further reduce NOx emissions in order to attain a pre-set state NOx (NOx) emission level by May 31, 2004. PEC is currently installing controls necessary to comply with the rule. Capital expenditures to meet these measures in North and South Carolina could reach approximately $370 million, which has not been adjusted for inflation. PEC has spent approximately $258 million to date related to these expenditures. Increased operation and maintenance costs relating to the NOx SIP Call are not expected to be material to PEC's results of operations. Further controls are anticipated as electricity demand increases. PEC cannot predict the outcome of this matter.

In July 1997, the EPA issued final regulations establishing a new 8-hour ozone standard. In October 1999, the District of Columbia Circuit Court of Appeals ruled against the EPA with regard to the federal 8-hour ozone standard. The U.S. Supreme Court has upheld, in part, the District of Columbia Circuit Court of Appeals decision. Designation of areas that do not attain the standard is proceeding, and further litigation and rulemaking on this and other aspects of the standard are anticipated. North Carolina adopted the federal 8-hour ozone standard and is proceeding with the implementation process. North Carolina has promulgated final regulations, which will require PEC to install NOx controls under the State's 8-hour standard. The costs of those controls are included in the $370 million cost estimate above. However, further technical analysis and rulemaking may result in a requirement for additional controls at some units. PEC cannot predict the outcome of this matter.

The EPA published a final rule approving petitions under Section 126 of the Clean Air Act. This rule as originally promulgated required certain sources to make reductions in NOx emissions by May 1, 2003. The final rule also includes a set of regulations that affect NOx emissions from sources included in the petitions. The North Carolina coal-fired electric generating plants are included in these petitions. Acceptable state plans under the NOx SIP Call can be approved in lieu of the final rules the EPA approved as part of the 126 petitions. PEC, other utilities, trade organizations and other states participated in litigation challenging the EPA's action. On May 15, 2001, the District of Columbia Circuit Court of Appeals ruled in favor of the EPA, which will require North Carolina to make reductions in NOx emissions by May 1, 2003. However, the Court in its May 15th decision rejected the EPA's methodology for estimating the future growth factors the EPA used in calculating the emissions limits for utilities. In August 2001, the Court granted a request by PEC and other utilities to delay the implementation of the 126 Rule for electric generating units pending resolution by the EPA of the growth factor issue. The Court's order tolls the three-year compliance period (originally set to end on May 1, 2003) for electric generating units as of May 15, 2001. On April 30, 2002, the EPA published a final rule harmonizing the dates for the Section 126 Rule and the NOx SIP Call. In addition, the EPA determined in this rule that the future growth factor estimation methodology was appropriate. The new compliance date for all affected sources is now May 31, 2004, rather than May 1, 2003. The EPA has approved North Carolina's NOx SIP Call rule and has indicated it will rescind the Section 126 rule in a future rulemaking. PEC expects a favorable outcome of this matter.

In June 2002, legislation was enacted in North Carolina requiring the state's electric utilities to reduce the emissions of NOx and SO2 from coal-fired power plants. PEC expects its capital costs to meet these emission targets will be approximately $813 million by 2013. PEC has expended approximately $30 million of these capital costs through December 31, 2003. PEC currently has approximately 5,100 MW of coal-fired generation in North Carolina that is affected by this legislation. The legislation requires the emissions reductions to be completed in phases by 2013, and applies to each utility's total system rather than setting requirements for individual power plants. The legislation also freezes the utilities' base rates for five years unless there are extraordinary events beyond the control of the utilities or unless the utilities persistently earn a return substantially in excess of the rate of return established and found reasonable by the NCUC in the utilities' last general rate case. Further, the legislation allows the utilities to recover from their retail customers the projected capital costs during the first seven years of the 10-year compliance period beginning on January 1, 2003. The utilities must recover at least 70% of their projected capital costs during the five-year rate freeze period. Pursuant to the law, PEC entered into an agreement with the state of North Carolina to transfer to the state all future emissions allowances it generates from over-complying with the federal emission limits when these units are completed. The law also requires the state to undertake a study of mercury and carbon dioxide emissions in North Carolina. Operation and maintenance costs will increase due to the additional personnel, materials and general maintenance associated with the equipment. Operation and maintenance expenses are recoverable through base rates, rather than as part of this program. PEC cannot predict the future regulatory interpretation, implementation or impact of this law.

In 1997, the EPA's Mercury Study Report and Utility Report to Congress conveyed that mercury is not a risk to the average American and expressed uncertainty about whether reductions in mercury emissions from coal-fired power plants would reduce human exposure. Nevertheless, EPA determined in 2000 that regulation of mercury emissions from coal-fired power plants was appropriate. In 2003, the EPA proposed two alternative control plans that would limit mercury emissions from coal-fired power plants. The first, a Maximum Available Control Technology (MACT) standard applicable to every coal-fired plant, would require compliance in 2008. The second, a national mercury cap and trade program, would require limits to be met in two phases, 2010 and 2018. The mercury rule is expected to become final in December 2004. Achieving compliance with either proposal could involve significant capital costs which could be material to PEC's consolidated financial position or results of operations. PEC cannot predict the outcome of this matter.

In conjunction with the proposed mercury rule, the EPA proposed to regulate nickel emissions from residual oil-fired units. The agency estimates the proposal will reduce national nickel emissions to approximately 103 tons. The rule is expected to become final in December 2004.

In December 2003, the EPA released its proposed Interstate Air Quality Rule (commonly known as the Fine Particulate Transport Rule and/or the Regional Transport Rule). The EPA's proposal requires 28 jurisdictions, including North Carolina, South Carolina, Georgia and Florida, to further reduce NOx and SO2 emissions in order to attain pre-set NOx and SO2 emissions levels (which have not yet been determined). The rule is expected to become final in 2004. The installation of controls necessary to comply with the rule could involve significant capital costs.

Water Quality

As a result of the operation of certain control equipment needed to address the air quality issues outlined above, new wastewater streams will be generated at the applicable facilities. Integration of these new wastewater streams into the existing wastewater treatment processes may result in permitting, construction and treatment challenges to PEC in the immediate and extended future.

After many years of litigation and settlement negotiations the EPA published regulations in February 2004 for the implementation of Section 316(b) of the Clean Water Act. The purpose of these regulations is to minimize adverse environmental impacts caused by cooling water intake structures and intake systems. Over the next several years these regulations will impact the larger base load generation facilities and may require the facilities to mitigate the effects to aquatic organisms by constructing intake modifications or undertaking other restorative activities. Substantial costs could be incurred by the facilities in order to comply with the new regulation. The Company cannot predict the outcome and impacts to the facilities at this time.

Other Environmental Matters

The Kyoto Protocol was adopted in 1997 by the United Nations to address global climate change by reducing emissions of carbon dioxide and other greenhouse gases. The United States has not adopted the Kyoto Protocol, however, a number of carbon dioxide emissions control proposals have been advanced in Congress and by the Bush administration. The Bush administration favors voluntary programs. Reductions in carbon dioxide emissions to the levels specified by the Kyoto Protocol and some legislative proposals could be materially adverse to PEC's consolidated financial position or results of operations if associated costs cannot be recovered from customers. PEC favors the voluntary program approach recommended by the administration and is evaluating options for the reduction, avoidance, and sequestration of greenhouse gases. However, PEC cannot predict the outcome of this matter.

2. As required under the Nuclear Waste Policy Act of 1982, PEC entered into a contract with the DOE under which the DOE agreed to begin taking spent nuclear fuel by no later than January 31, 1998. All similarly situated utilities were required to sign the same standard contract.

In April 1995, the DOE issued a final interpretation that it did not have an unconditional obligation to take spent nuclear fuel by January 31, 1998. In Indiana Michigan Power v. DOE, the Court of Appeals vacated the DOE's final interpretation and ruled that the DOE had an unconditional obligation to begin taking spent nuclear fuel. The Court did not specify a remedy because the DOE was not yet in default.

After the DOE failed to comply with the decision in Indiana Michigan Power v. DOE, a group of utilities petitioned the Court of Appeals in Northern States Power (NSP) v. DOE, seeking an order requiring the DOE to begin taking spent nuclear fuel by January 31, 1998. The DOE took the position that its delay was unavoidable, and the DOE was excused from performance under the terms and conditions of the contract. The Court of Appeals did not order the DOE to begin taking spent nuclear fuel, stating that the utilities had a potentially adequate remedy by filing a claim for damages under the contract.

After the DOE failed to begin taking spent nuclear fuel by January 31, 1998, a group of utilities filed a motion with the Court of Appeals to enforce the mandate in NSP v. DOE. Specifically, this group of utilities asked the Court to permit the utilities to escrow their waste fee payments, to order the DOE not to use the waste fund to pay damages to the utilities, and to order the DOE to establish a schedule for disposal of spent nuclear fuel. The Court denied this motion based primarily on the grounds that a review of the matter was premature, and that some of the requested remedies fell outside of the mandate in NSP v. DOE.

Subsequently, a number of utilities each filed an action for damages in the Federal Court of Claims. The U.S. Circuit Court of Appeals (Federal Circuit) ruled that utilities may sue the DOE for damages in the Federal Court of Claims instead of having to file an administrative claim with DOE.

On January 14, 2004, PEC filed a complaint with the United States Court of Federal Claims against the United States of America (Department of Energy) claiming that the DOE breached the Standard Contract for Disposal of Spent Nuclear Fuel by failing to accept spent nuclear fuel from various Progress Energy facilities on or before January 31, 1998. Damages due to DOE's breach will likely exceed $100 million. Similar suits have been initiated by over two dozen other utilities.

In July 2002, Congress passed an override resolution to Nevada's veto of DOE's proposal to locate a permanent underground nuclear waste storage facility at Yucca Mountain, Nevada. DOE plans to submit a license application for the Yucca Mountain facility by the end of 2004. On November 5, 2003, Congressional negotiators approved $580 million for fiscal year 2004 for the Yucca Mountain project, $123 million more than the previous year. PEC cannot predict the outcome of this matter.

With certain modifications and additional approval by the NRC, PEC's spent nuclear fuel storage facilities will be sufficient to provide storage space for spent fuel generated on its system through the expiration of the current operating licenses for all of its nuclear generating units. Subsequent to the expiration of these licenses, dry storage may be necessary. PEC obtained NRC approval in December 2000 to use additional storage space at the Harris Plant.

3. In August 2003, PEC was served as a co-defendant in a purported class action lawsuit styled as Collins v. Duke Energy Corporation et al, Civil action No. 03CP404050, in South Carolina's Circuit Court of Common Pleas for the Fifth Judicial Circuit. PEC is one of three electric utilities operating in South Carolina named in the suit. The plaintiffs are seeking damages for the alleged improper use of electric easements but have not asserted a dollar amount for their damage claims. The complaint alleges that the licensing of attachments on electric utility poles, towers and other structures to non-utility third parties or telecommunication companies for other than the electric utilities' internal use along the electric right-of-way constitutes a trespass.

In September 2003, PEC filed a motion to dismiss all counts of the complaint on substantive and procedural grounds. In October 2003, the plaintiffs filed a motion to amend their complaint. PEC believes the amended complaint asserts the same factual allegations as are in the original complaint and also seeks money damages and injunctive relief.

The court has not yet held any hearings or made any rulings in this case. In November 2003, PEC filed a motion to dismiss the plaintiffs' first amended complaint. PEC cannot predict the outcome of the outcome of this matter, but will vigorously defend against the allegations.

4. PEC is involved in various litigation matters in the ordinary course of business, some of which involve substantial amounts. Where appropriate, accruals have been made in accordance with SFAS No. 5, "Accounting for Contingencies," to provide for such matters. In the opinion of management, the final disposition of pending litigation would not have a material adverse effect on PEC's consolidated results of operations or financial position.

INDEPENDENT AUDITORS' REPORT

TO THE BOARD OF DIRECTORS AND SHAREHOLDER OF CAROLINA POWER & LIGHT COMPANY d/b/a PROGRESS ENERGY CAROLINAS, INC.:

We have audited the consolidated balance sheets of Carolina Power & Light Company d/b/a Progress Energy Carolinas, Inc. and its subsidiaries (PEC) at December 31, 2003 and 2002, and the related consolidated statements of income and comprehensive income, retained earnings, and cash flows for each of the three years in the period ended December 31, 2003 and have issued our report thereon dated February 20, 2004 (which express an unqualified opinion and includes an explanatory paragraph concerning the adoption of new accounting principles in 2003); such consolidated financial statements and report are included herein. Our audits also included the consolidated financial statement schedule of PEC listed in Item 8. This consolidated financial statement schedule is the responsibility of PEC's management. Our responsibility is to express an opinion based on our audits. In our opinion, such consolidated financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/ DELOITTE & TOUCHE LLP
Raleigh, North Carolina
February 20, 2004

CAROLINA POWER & LIGHT COMPANY
d/b/a PROGRESS ENERGY CAROLINAS, INC.
CONSOLIDATED INTERIM FINANCIAL STATEMENTS
September 30, 2004

UNAUDITED CONSOLIDATED STATEMENTS of INCOME

(in millions)	Three Months Ended September 30 2004	2003	Nine Months Ended September 30 2004	2003
Operating Revenues				
Electric	**$ 1,014**	$ 1,010	**$ 2,776**	$ 2,752
Diversified business	**-**	2	**1**	8
Total Operating Revenues	**1,014**	1,012	**2,777**	2,760
Operating Expenses				
Fuel used in electric generation	**220**	234	**637**	637
Purchased power	**96**	98	**238**	240
Operation and maintenance	**197**	205	**632**	605
Depreciation and amortization	**139**	135	**393**	416
Taxes other than on income	**44**	45	**132**	124
Diversified business	**-**	-	**-**	3
Total Operating Expenses	**696**	717	**2,032**	2,025
Operating Income	**318**	295	**745**	735
Other Income (Expense)				
Interest income	**-**	1	**2**	4
Other, net	**7**	(4)	**(1)**	(14)
Total Other Income (Expense)	**7**	(3)	**1**	(10)
Interest Charges				
Interest charges	**50**	47	**146**	145
Allowance for borrowed funds used during construction	**(1)**	1	**(2)**	(1)
Total Interest Charges, Net	**49**	48	**144**	144
Income before Income Tax	**276**	244	**602**	581
Income Tax Expense	**101**	87	**216**	200
Net Income	**$ 175**	$ 157	**$ 386**	$ 381
Preferred Stock Dividend Requirement	**1**	1	**2**	2
Earnings for Common Stock	**$ 174**	$ 156	**$ 384**	$ 379

See Notes to Consolidated Interim Financial Statements.

CAROLINA POWER & LIGHT COMPANY
d/b/a PROGRESS ENERGY CAROLINAS, INC.
UNAUDITED CONSOLIDATED BALANCE SHEETS

(in millions)	September 30 2004	December 31 2003
ASSETS		
Utility Plant		
Utility plant in service	$ 13,563	$ 13,331
Accumulated depreciation	(5,499)	(5,306)
Utility plant in service, net	8,064	8,025
Held for future use	5	5
Construction work in progress	297	306
Nuclear fuel, net of amortization	169	159
Total Utility Plant, Net	8,535	8,495
Current Assets		
Cash and cash equivalents	18	238
Accounts receivable	266	265
Unbilled accounts receivable	135	145
Receivables from affiliated companies	39	27
Inventory	381	348
Deferred fuel cost	170	113
Prepayments and other current assets	69	82
Total Current Assets	1,078	1,218
Deferred Debits and Other Assets		
Regulatory assets	498	477
Nuclear decommissioning trust funds	554	505
Miscellaneous other property and investments	166	169
Other assets	135	118
Total Deferred Debits and Other Assets	1,353	1,269
Total Assets	$ 10,966	$ 10,982
CAPITALIZATION AND LIABILITIES		
Common Stock Equity		
Common stock without par value, authorized 200 million shares, 160 million shares issued and outstanding	$ 1,973	$ 1,953
Unearned ESOP common stock	(76)	(89)
Accumulated other comprehensive loss	(9)	(7)
Retained earnings	1,338	1,380
Total Common Stock Equity	3,226	3,237
Preferred Stock - Not Subject to Mandatory Redemption	59	59
Long-Term Debt, Net	2,749	3,086
Total Capitalization	6,034	6,382
Current Liabilities		
Current portion of long-term debt	300	300
Accounts payable and accrued liabilities	248	188
Payables to affiliated companies	89	136
Notes payable to affiliated companies	-	25
Interest accrued	58	64
Short-term obligations	146	4
Other current liabilities	251	166
Total Current Liabilities	1,092	883
Deferred Credits and Other Liabilities		
Accumulated deferred income taxes	1,103	1,125
Accumulated deferred investment tax credits	142	148
Regulatory liabilities	1,240	1,149
Asset retirement obligations	973	932
Other liabilities	382	363
Total Deferred Credits and Other Liabilities	3,840	3,717
Commitments and Contingencies (Note 11)		
Total Capitalization and Liabilities	$ 10,966	$ 10,982

See Notes to Consolidated Interim Financial Statements.

CAROLINA POWER & LIGHT COMPANY
d/b/a PROGRESS ENERGY CAROLINAS, INC.
UNAUDITED CONSOLIDATED STATEMENTS of CASH FLOWS

(in millions)	Nine Months Ended September 30 2004	2003
Operating Activities		
Net income	**$ 386**	$ 381
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	**460**	486
Deferred income taxes	**(20)**	(46)
Investment tax credit	**(6)**	(8)
Deferred fuel (credit) cost	**(57)**	11
Cash provided (used) by changes in operating assets and liabilities:		
Accounts receivable	**7**	38
Inventories	**9**	17
Prepayments and other current assets	**5**	11
Accounts payable	**(35)**	(85)
Other current liabilities	**78**	97
Other	**62**	59
Net Cash Provided by Operating Activities	**889**	961
Investing Activities		
Gross property additions	**(363)**	(347)
Proceeds from sale of assets and investments	**5**	26
Nuclear fuel additions	**(63)**	(46)
Contributions to nuclear decommissioning trust	**(26)**	(26)
Other investing activities	**5**	(1)
Net Cash Used in Investing Activities	**(442)**	(394)
Financing Activities		
Issuance of long-term debt, net	**-**	588
Net increase (decrease) in short-term obligations	**142**	(438)
Net change in intercompany notes	**(42)**	(73)
Retirement of long-term debt	**(339)**	(269)
Dividends paid to parent	**(426)**	(328)
Dividends paid on preferred stock	**(2)**	(2)
Net Cash Used in Financing Activities	**(667)**	(522)
Net (Decrease) Increase in Cash and Cash Equivalents	**(220)**	45
Cash and Cash Equivalents at Beginning of Period	**238**	18
Cash and Cash Equivalents at End of Period	**$ 18**	$ 63
Supplemental Disclosures of Cash Flow Information		
Cash paid during the year – interest (net of amount capitalized)	**$ 146**	$ 151
income taxes (net of refunds)	**$ 200**	$ 210

See Notes to Consolidated Interim Financial Statements.

CAROLINA POWER & LIGHT COMPANY
d/b/a PROGRESS ENERGY CAROLINAS, INC.
NOTES TO CONSOLIDATED INTERIM FINANCIAL STATEMENTS

1. ORGANIZATION AND BASIS OF PRESENTATION

A. Organization

Carolina Power & Light Company d/b/a Progress Energy Carolinas, Inc. (PEC) is a public service corporation primarily engaged in the generation, transmission, distribution and sale of electricity in portions of North Carolina and South Carolina. Through its wholly-owned subsidiaries, PEC is also involved in nonregulated business activities. PEC is a wholly-owned subsidiary of Progress Energy, Inc. (the Company or Progress Energy). The Company is a registered holding company under the Public Utility Holding Company Act of 1935 (PUHCA). Both the Company and its subsidiaries are subject to the regulatory provisions of PUHCA. PEC is regulated by the North Carolina Utilities Commission (NCUC), the Public Service Commission of South Carolina (SCPSC), the Federal Energy Regulatory Commission (FERC) and the United States Nuclear Regulatory Commission (NRC).

B. Basis of Presentation

These financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and with the instructions to Form 10-Q and Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for annual statements. Because the accompanying consolidated interim financial statements do not include all of the information and footnotes required by GAAP, they should be read in conjunction with the audited financial statements for the period ended December 31, 2003 and notes thereto included in PEC's Form 10-K for the year ended December 31, 2003.

PEC collects from customers certain excise taxes, which include gross receipts tax, franchise taxes, and other excise taxes, levied by the state or local government upon the customers. PEC accounts for excise taxes on a gross basis. For the three month periods ended September 30, 2004 and 2003, excise taxes of approximately $25 million are included in taxes other than on income in the accompanying Consolidated Statements of Income. For the nine month periods ended September 30, 2004 and 2003, excise taxes of approximately $70 million and $65 million, respectively, are included in taxes other than on income in the accompanying Consolidated Statements of Income. These approximate amounts are also included in utility revenues.

The amounts included in the consolidated interim financial statements are unaudited but, in the opinion of management, reflect all normal recurring adjustments necessary to fairly present PEC's financial position and results of operations for the interim periods. Due to seasonal weather variations and the timing of outages of electric generating units, especially nuclear-fueled units, the results of operations for interim periods are not necessarily indicative of amounts expected for the entire year or future periods.

In preparing financial statements that conform with GAAP, management must make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and amounts of revenues and expenses reflected during the reporting period. Actual results could differ from those estimates. Certain amounts for 2003 have been reclassified to conform to the 2004 presentation.

C. Stock-Based Compensation

PEC measures compensation expense for stock options as the difference between the market price of its common stock and the exercise price of the option at the grant date. The exercise price at which options are granted by the Company equals the market price at the grant date, and accordingly, no compensation expense has been recognized for stock option grants. For purposes of the pro forma disclosures required by Statement of Financial Account Standards (SFAS) No. 148, "Accounting for Stock-Based Compensation – Transition and Disclosure – an Amendment of FASB Statement No. 123" (SFAS No. 148), the estimated fair value of the Company's stock options is amortized to expense over the options' vesting period. The following table illustrates the effect on net income and earnings per share if the fair value method had been applied to all outstanding and unvested awards in each period:

(in millions)	Three Months Ended September 30 2004	2003	Nine Months Ended September 30 2004	2003
Earnings for Common Stock, as reported	**$ 174**	$ 156	**$ 384**	$ 379
Deduct: Total stock option expense determined under fair value method for all awards, net of related tax effects	**2**	2	**5**	4
Pro forma net income	**$ 172**	$ 154	**$ 379**	$ 375

PEC expects to begin expensing stock options in 2005, either by adopting SFAS No. 123, as amended by SFAS No. 148, or by adopting new FASB guidance on accounting for stock-based compensation that is expected to be issued in late 2004 and become effective July 1, 2005. In 2004, however, the Company made the decision to cease granting stock options and intends to replace that compensation program with other programs. Therefore, the amount of stock option expense expected to be recorded in 2005 is below the amount that would have been recorded if the stock option program had continued. If stock option expense is recorded for the full year 2005, approximately $3 million of pre-tax expense would be recorded.

D. Consolidation of Variable Interest Entities

PEC consolidates all voting interest entities in which it owns a majority voting interest and all variable interest entities for which it is the primary beneficiary in accordance with FASB Interpretation No. 46R, "Consolidation of Variable Interest Entities – an Interpretation of ARB No. 51" (FIN No. 46R). PEC is the primary beneficiary of and consolidates two limited partnerships that qualify for federal affordable housing and historic tax credits under Section 42 of the Internal Revenue Code. As of September 30, 2004, the total assets of the two entities were $39 million, the majority of which are collateral for the entities' obligations and are included in other current assets and miscellaneous other property in the Consolidated Balance Sheet.

PEC is the primary beneficiary of a limited partnership which invests in 17 low-income housing partnerships that qualify for federal and state tax credits. PEC has requested but has not received all the necessary information to determine the primary beneficiary of the limited partnership's underlying 17 partnership investments, and has applied the information scope exception in FIN No. 46R, paragraph 4(g) to the 17 partnerships. PEC has no direct exposure to loss from the 17 partnerships; PEC's only exposure to loss is from its investment of less than $1 million in the consolidated limited partnership. PEC will continue its efforts to obtain the necessary information to fully apply FIN No. 46R to the 17 partnerships. PEC believes that if the limited partnership is determined to be the primary beneficiary of the 17 partnerships, the effect of consolidating the 17 partnerships would not be significant to PEC's Consolidated Balance Sheets.

PEC has variable interests in two power plants resulting from long-term power purchase contracts. PEC has requested the necessary information to determine if the counterparties are variable interest entities or to identify the primary beneficiaries. Both entities declined to provide PEC with the necessary financial information, and PEC has applied the information scope exception in FIN No. 46R, paragraph 4(g). PEC's only significant exposure to variability from these contracts results from fluctuations in the market price of fuel used by the two entities' plants to produce the power purchased by PEC. PEC is able to recover these fuel costs under its fuel clause. Total purchases from these counterparties were approximately $46 million and $43 million in the first nine months of 2004 and 2003, respectively. PEC will continue its efforts to obtain the necessary information to fully apply FIN No. 46R to these contracts. The combined generation capacity of the two entities' power plants is approximately 880 MW. PEC believes that if it is determined to be the primary beneficiary of these two entities, the effect of consolidating the entities would result in increases to total assets, long-term debt and other liabilities, but would have an insignificant or no impact on PEC's common stock equity, net earnings, or cash flows. However, because PEC has not received any financial information from these two counterparties, the impact cannot be determined at this time.

PEC also has interests in several other variable interest entities for which PEC is not the primary beneficiary. These arrangements include investments in approximately 22 limited partnerships, limited liability corporations and venture capital funds and two building leases with special-purpose entities. The aggregate maximum loss exposure at September 30, 2004, that PEC could be required to record in its income statement as a result of these arrangements totals approximately $24 million. The creditors of these variable interest entities do not have recourse to the general credit of PEC in excess of the aggregate maximum loss exposure.

2. NEW ACCOUNTING STANDARDS

In December 2003, the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (Medicare Act) was signed into law. In accordance with guidance issued by the FASB in FASB Staff Position 106-2, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug Improvement and Modernization Act of 2003" (FASB Staff Position 106-2), PEC elected to defer accounting for the effects of the Medicare Act due to uncertainties regarding the effects of the implementation of the Medicare Act and the accounting for certain provisions of the Medicare Act. In May 2004, the FASB issued definitive accounting guidance for the Medicare Act in FASB Staff Position 106-2, which was effective for PEC in the third quarter of 2004. FASB Staff Position 106-2 results in the recognition of lower other post retirement employee benefit (OPEB) costs to reflect prescription drug-related federal subsidies to be received under the Medicare Act. As a result of the Medicare Act, PEC's accumulated postretirement benefit obligation as of January 1, 2004 was reduced by approximately $42 million and PEC's 2004 net periodic cost will be reduced by approximately $7 million. PEC recorded $5 million of the net periodic cost reduction in the quarter ended September 30, 2004. Prior quarters were not restated due to the immateriality of the adjustments.

3. HURRICANE-RELATED COSTS

Hurricanes Charley and Ivan struck portions of PEC's service territory during the third quarter of 2004. PEC has estimated restoration costs of $13 million, of which $12 million was charged to operation and maintenance expense and $1 million was charged to capital expenditures.

PEC does not have an on-going regulatory mechanism to recover storm costs and, therefore, hurricane restoration costs recorded in the third quarter of 2004 were charged to operations and maintenance expenses or capital expenditures based on the nature of the work performed. In connection with other storms, PEC has previously sought and received permission from the North Carolina Utilities Commission (NCUC) and the Public Service Commission of South Carolina (SCPSC) to defer storm expenses and amortize them over a five-year period. PEC is planning to seek deferral of 2004 storm costs from the NCUC in the fourth quarter of 2004.

4. REGULATORY MATTERS

A. Retail Rate Matters

PEC has exclusively utilized external funding for its decommissioning liability since 1994. Prior to 1994, PEC retained funds internally to meet its decommissioning liability. An NCUC order issued in February 2004 found that by January 1, 2008 PEC must begin transitioning these amounts to external funds. The transition of $131 million must be completed by December 31, 2017, and at least 10% must be transitioned each year.

PEC filed with the SCPSC seeking permission to defer expenses incurred from the first quarter 2004 winter storm. The SCPSC approved PEC's request to defer the costs and amortize them ratably over five years beginning in January 2005. Approximately $10 million related to storm costs incurred during the first quarter of 2004 was deferred in that quarter.

During the first quarter of 2004, PEC met the requirements of both the NCUC and the SCPSC for the implementation of a depreciation study which allowed the utility to reduce the rates used to calculate depreciation expense. As a result, depreciation expense decreased $7 million for the three months ended September 30, 2004 compared to the prior year quarter and decreased $17 million for the nine months ended September 30, 2004 compared to the prior year nine month period.

In October 2004, PEC filed a revised depreciation study with the NCUC and SCPSC supporting a reduction in annual depreciation expense of approximately $47 million. The reduction is due solely to extended lives at each of PEC's nuclear units. The new depreciation rates are proposed to be effective January 1, 2004.

PEC obtained SCPSC and NCUC approval of fuel factors in annual fuel-adjustment proceedings. The SCPSC approved PEC's petition to leave billing rates unchanged from the prior year by order issued in March 2004. The NCUC approved an annual increase of $62 million by order issued in September 2004.

B. Regional Transmission Organizations

In 2000, the FERC issued Order No. 2000 on RTOs, which set minimum characteristics and functions that RTOs must meet, including independent transmission service. In July 2002, the FERC issued its Notice of Proposed Rulemaking in Docket No. RM01-12-000, Remedying Undue Discrimination through Open Access Transmission Service and Standard Electricity Market Design (SMD NOPR). If adopted as proposed, the rules set forth in the SMD NOPR would materially alter the manner in which transmission and generation services are provided and paid for. In April 2003, the FERC released a White Paper on the Wholesale Market Platform. The White Paper provides an overview of what the FERC currently intends to include in a final rule in the SMD NOPR docket. The White Paper retains the fundamental and most protested aspects of SMD NOPR, including mandatory RTOs and the FERC's assertion of jurisdiction over certain aspects of retail service. The FERC has not yet issued a final rule on SMD NOPR. PEC cannot predict the outcome of these matters or the effect that they may have on the GridSouth proceedings currently ongoing before the FERC. It is unknown what impact the future proceedings will have on PEC's earnings, revenues or prices.

PEC has $33 million invested in GridSouth related to startup costs at September 30, 2004. PEC expects to recover these startup costs in conjunction with the GridSouth original structure or in conjunction with any alternate combined transmission structures that emerge.

C. Implementation of SFAS No. 143

In connection with the implementation of SFAS No. 143, "Accounting for Asset Retirement Obligations," in 2003, PEC filed a request with the NCUC requesting deferral of the difference between expense pursuant to SFAS No. 143 and expense as previously determined by the NCUC. The NCUC granted the deferral of the January 1, 2003 cumulative adjustment. Because the clean air legislation discussed in Note 11 under "Air Quality" contained a prohibition against cost deferrals unless certain criteria are met, the NCUC denied the deferral of the ongoing effects. Therefore, PEC ceased deferral of the ongoing effects during the second quarter for the six months ended June 30, 2003 related to its North Carolina retail jurisdiction. Pre-tax income for the three and six months ended June 30, 2003 increased by approximately $14 million, which represents a decrease in non-ARO cost of removal expense, partially offset by an increase in decommissioning expense. The Company provided additional information to the NCUC that demonstrated that deferral of the ongoing effects should also be allowed. In August 2003, the NCUC revised its decision and approved the deferral of the ongoing effects of SFAS No. 143 at which time the $14 million impact was reversed.

D. FERC Market Power Mitigation

A FERC order issued in November 2001 on certain unaffiliated utilities' triennial market based wholesale power rate authorization updates required certain mitigation actions that those utilities would need to take for sales/purchases within their control areas and required those utilities to post information on their websites regarding their power systems' status. As a result of a request for rehearing filed by certain market participants, FERC issued an order delaying the effective date of the mitigation plan until after a planned technical conference on market power determination. In December 2003, the FERC issued a staff paper discussing alternatives and held a technical conference in January 2004. In April 2004, the FERC issued two orders concerning utilities' ability to sell wholesale electricity at market based rates. In the first order, the FERC adopted two new interim screens for assessing potential generation market power of applicants for wholesale market based rates, and described additional analyses and mitigation measures that could be presented if an applicant does not pass one of these interim screens. In July 2004, the FERC issued an order on rehearing affirming its conclusions in the April order. In the second order, the FERC initiated a rulemaking to consider whether the FERC's current methodology for determining whether a public utility should be allowed to sell wholesale electricity at market-based rates should be modified in any way. Management is unable to predict the outcome of these actions by the FERC or their effect on future results of operations and cash flows. However, PEC does not anticipate that its current operations would be impacted materially if they were unable to sell power at market-based rates in their respective control areas.

Due to PEC's failure of one of the two interim market power screens, on August 12, 2004, PEC notified the FERC that it would revise its Market Based Rate tariff to restrict it to sales outside PEC's control area and file a new cost based tariff for sales within PEC's control area that incorporates the FERC's default cost based rate methodologies for sales of one year or less. PEC anticipates making this filing by year-end.

5. COMPREHENSIVE INCOME

Comprehensive income for the three months ended September 30, 2004 and 2003 was $170 million and $162 million, respectively. Comprehensive income for the nine months ended September 30, 2004 and 2003 was $384 million and $385 million, respectively. Changes in other comprehensive income for the periods consisted primarily of changes in fair value of derivatives used to hedge cash flows related to interest on long-term debt.

6. FINANCING ACTIVITIES

Between October 19, 2004 and November 1, 2004, PEC borrowed a net total of $115 million under certain long-term revolving credit facilities. In addition, PEC borrowed $90 million under its short-term credit facility. The credit facilities contain various cross default and other acceleration provisions. PEC's long-term credit facilities were arranged through a syndication of financial institutions and support its commercial paper programs. The borrowed funds will be used to pay off maturing commercial paper and for other cash needs. This action was taken due to the uncertain impact on PEC's ability to access the commercial paper markets resulting from recent ratings actions taken by Standard and Poor's ("S&P") credit rating agency and Moody's Investor Services ("Moody's").

On October 19, 2004, S&P changed Progress Energy's outlook from stable to negative. S&P cited the uncertainties regarding the timing of the recovery of hurricane costs, the Company's debt reduction plans, and the IRS audit of the Company's Earthco synthetic fuels facilities as the reasons for the change in outlook. On October 25, 2004, S&P reduced the short-term debt rating of PEC to A-3 from A-2, as a result of their change in outlook discussed above.

On October 20, 2004, Moody's changed its outlook for Progress Energy from stable to negative. PEC's ratings were affirmed by Moody's.

The changes by S&P do not trigger any debt or guarantee collateral requirements, nor do they have any material impact on the overall liquidity of PEC. To date, PEC's access to the commercial paper markets has not been materially impacted by the rating agencies' actions. However, the changes are expected to increase the interest rate incurred on its short-term borrowings by 0.25% to 0.875%.

On July 28, 2004, PEC extended its $165 million 364-day line of credit, which was scheduled to expire on July 29, 2004. The line of credit will expire on July 27, 2005.

On April 30, 2004, PEC redeemed $35 million of Darlington County 6.6% Series Pollution Control Bonds at 102.5% of par, $2 million of New Hanover County 6.3% Series Pollution Control Bonds at 101.5% of par, and $2 million of Chatham County 6.3% Series Pollution Control Bonds at 101.5% of par with cash from operations.

On January 15, 2004, PEC paid at maturity $150 million 5.875% First Mortgage Bonds with commercial paper proceeds. On April 15, 2004, PEC also paid at maturity $150 million 7.875% First Mortgage Bonds with commercial paper proceeds and cash from operations.

7. BENEFIT PLANS

PEC has a non-contributory defined benefit retirement (pension) plan for substantially all full-time employees. PEC also has supplementary defined benefit pension plans that provide benefits to higher-level employees. In addition to pension benefits, PEC provides contributory other postretirement benefits (OPEB), including certain health care and life insurance benefits, for retired employees who meet specified criteria. The components of the net periodic benefit cost for the three and nine months ended September 30 are:

Three Months Ended September 30 (in millions)	Pension Benefits		Other Postretirement Benefits	
	2004	2003	**2004**	2003
Service cost	**$ 6**	$ 6	**$ 1**	$ 2
Interest cost	**13**	14	**3**	5
Expected return on plan assets	**(18)**	(19)	**(1)**	(1)
Amortization, net	**-**	1	**-**	1
Net periodic cost	**$ 1**	$ 2	**$ 3**	$ 7

Nine Months Ended September 30 (in millions)	Pension Benefits		Other Postretirement Benefits	
	2004	2003	**2004**	2003
Service cost	**$ 18**	$ 17	**$ 5**	$ 5
Interest cost	**39**	38	**11**	11
Expected return on plan assets	**(52)**	(52)	**(3)**	(2)
Amortization, net	**1**	1	**2**	4
Net periodic cost	**$ 6**	$ 4	**$ 15**	$ 18

Net periodic costs for other postretirement benefits decreased during the three and nine months ended September 30, 2004 due to the implementation of FASB Staff Position 106-2. See discussion in Note 2 to the Consolidated Interim Financial Statements.

8. RISK MANAGEMENT ACTIVITIES AND DERIVATIVE TRANSACTIONS

Under its risk management policy, PEC may use a variety of instruments, including swaps, options and forward contracts, to manage exposure to fluctuations in commodity prices and interest rates. See Note 12 to the financial statements in Item 8 of the Annual Report on Form 10-K for the year ended December 31, 2003.

Nonhedging Derivatives

Nonhedging derivatives, primarily electricity and natural gas contracts, are entered into for economic hedging purposes. While management believes the economic hedges mitigate exposures to fluctuations in commodity prices, these instruments are not designated as hedges for accounting purposes and are monitored consistent with trading positions. Gains and losses from such contracts were not material during the nine months ending September 30, 2004, and PEC did not have material outstanding positions in such contracts at September 30, 2004.

Cash Flow Hedges

PEC uses cash flow hedging strategies to hedge variable interest rates on long-term and short-term debt and to hedge interest rates with regard to future fixed-rate debt issuances. As of September 30, 2004, PEC had $110 million notional amount of pay-fixed forward swaps to hedge its exposure to interest rates with regard to future issuances of debt and $26 million notional amount of pay-fixed forward starting swaps to hedge its exposure to interest rates with regard to an upcoming railcar lease. All the swaps have a computational period of ten years. These hedges had a fair value liability position of $2 million at September 30, 2004. PEC had no open cash flow hedges at December 31, 2003. The ineffective portion of interest rate cash flow hedges for the three and nine-month periods ending September 30, 2004 was not material to PEC's results of operations. As of September 30, 2004, PEC had $7 million of after-tax deferred losses in accumulated other comprehensive income (OCI), including amounts related to terminated hedges, of which $1 million are expected to be reclassified to earnings within the next 12 months. Due to the volatility of interest rates, the value in OCI is subject to change prior to its reclassification into earnings.

Fair Value Hedges

PEC uses fair value hedging strategies to manage its exposure to fixed interest rates on long-term debt. At September 30, 2004 and December 31, 2003, PEC had no open interest rate fair value hedges.

9. FINANCIAL INFORMATION BY BUSINESS SEGMENT

PEC's operations consist primarily of the PEC Electric segment which is engaged in the generation, transmission, distribution and sale of electric energy primarily in portions of North Carolina and South Carolina. These electric operations are subject to the rules and regulations of the FERC, the NCUC, the SCPSC and the NRC. PEC Electric also distributes and sells electricity to other utilities, primarily on the east coast of the United States.

The Other segment, whose operations are primarily in the United States, is made up of other nonregulated business areas and eliminations that do not separately meet the disclosure requirements of SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information."

The financial information for PEC segments for the three and nine months ended September 30, 2004 and 2003 is as follows:

Three Months Ended September 30	2004			2003		
(in millions)	PEC Electric	Other	Total	PEC Electric	Other	Total
Total revenues	**$ 1,014**	**$ -**	**$ 1,014**	$ 1,010	$ 2	$ 1,012
Earnings available for common	**175**	**(1)**	**174**	160	(4)	156

Nine Months Ended September 30	2004			2003		
(in millions)	PEC Electric	Other	Total	PEC Electric	Other	Total
Total revenues	**$ 2,776**	**$ 1**	**$ 2,777**	$ 2,752	$ 8	$ 2,760
Earnings available for common	**388**	**(4)**	**384**	383	(4)	379

No single customer accounted for 10% or more of unaffiliated revenues.

10. OTHER INCOME AND OTHER EXPENSE

Other income and expense includes interest income and other income and expense items as discussed below. The components of other, net as shown on the accompanying Consolidated Statements of Income are as follows:

(in millions)	Three Months Ended September 30 2004	2003	Nine Months Ended September 30 2004	2003
Other income				
Net financial trading gain	$ 3	$ -	$ 7	$ -
Nonregulated energy and delivery services income	2	3	9	9
Investment gains	2	1	3	2
AFUDC equity	1	(1)	3	1
Gain on sale of property	2	1	3	2
Other	2	2	3	5
Total other income	$ 12	$ 6	$ 28	$ 19
Other expense				
Nonregulated energy and delivery services expenses	$ 2	$ 2	$ 6	$ 6
Donations	1	1	5	4
Investment losses	-	2	2	12
Write-off of non-trade receivable	-	-	7	-
Loss on sale of property	-	2	-	2
Other	2	3	9	9
Total other expense	$ 5	$ 10	$ 29	$ 33
Other, net	$ 7	$ (4)	$ (1)	$ (14)

Net financial trading gains and losses represent non-asset-backed trades of electricity and gas. Nonregulated energy and delivery services include power protection services and mass market programs such as surge protection, appliance services and area light sales, and delivery, transmission and substation work for other utilities.

11. COMMITMENTS AND CONTINGENCIES

Contingencies and significant changes to the commitments discussed in Note 16 of the Company's 2003 Annual Report on Form 10-K are described below.

A. Guarantees

As a part of normal business, PEC enters into various agreements providing future financial or performance assurances to third parties, which are outside the scope of Financial Accounting Standards Board (FASB) Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others" (FIN 45). Such agreements include guarantees, standby letters of credit and surety bonds. At September 30, 2004, management does not believe conditions are likely for significant performance under these guarantees. To the extent liabilities are incurred as a result of the activities covered by the guarantees, such liabilities are included in the accompanying Consolidated Balance Sheets. At September 30, 2004, PEC had no guarantees issued on behalf of unconsolidated subsidiaries or other third parties.

B. Insurance

PEC is insured against public liability for a nuclear incident up to $10.8 billion per occurrence. Under the current provisions of the Price Anderson Act, which limits liability for accidents at nuclear plants, PEC, as an owner of nuclear units, can be assessed a portion of any third-party liability claims arising from an accident at any commercial nuclear power plant in the United States. In the event that public liability claims from an insured nuclear incident exceed $300 million (currently available through commercial insurers), PEC would be subject to assessments of up to $101 million for each reactor owned per occurrence. Payment of such assessments would be made over time as necessary to limit the payment in any one year to no more than $10 million per reactor owned. Congress is considering revisions to the Price Anderson Act that could include increased limits and assessments per reactor owned. The final outcome of this matter cannot be predicted at this time.

PEC self-insures its transmission and distribution lines against loss due to storm damage and other natural disasters.

C. Claims and Uncertainties

PEC is subject to federal, state and local regulations addressing hazardous and solid waste management, air and water quality and other environmental matters. See Note 16D to the financial statements in Item 8 of the Form 10-K for the year ended December 31, 2003.

Hazardous and Solid Waste Management

Various organic materials associated with the production of manufactured gas, generally referred to as coal tar, are regulated under federal and state laws. The principal regulatory agency that is responsible for a specific former manufactured gas plant (MGP) site depends largely upon the state in which the site is located. There are several MGP sites to which PEC has some connection. In this regard, PEC and other potentially responsible parties (PRPs) are participating in, investigating and, if necessary, remediating former MGP sites with several regulatory agencies, including, but not limited to, the U.S. Environmental Protection Agency (EPA) and the North Carolina Department of Environment and Natural Resources, Division of Waste Management (DWM). In addition, PEC is periodically notified by regulators such as the EPA and various state agencies of its involvement or potential involvement in sites, other than MGP sites, that may require investigation and/or remediation.

PEC has filed claims with its general liability insurance carriers to recover costs arising from actual or potential environmental liabilities. All claims have been settled other than with insolvent carriers. These settlements have not had a material effect on the consolidated financial position or results of operations.

PEC is also currently in the process of assessing potential costs and exposures at other environmentally impaired sites. As the assessments are developed and analyzed, PEC will accrue costs for the sites to the extent the costs are probable and can be reasonably estimated.

There are nine former MGP sites and other sites associated with PEC that have required or are anticipated to require investigation and/or remediation costs. PEC received insurance proceeds to address costs associated with environmental liabilities related to its involvement with some sites. All eligible expenses related to these are charged against a specific fund containing these proceeds. At December 31, 2003, the balance in the fund was $9 million. During the nine months ended September 30, 2004, PEC spent approximately $2 million related to environmental remediation. The remaining balance in the fund at September 30, 2004 was $7 million. At September 30, 2004, PEC had an accrual of $9 million recorded for environmental liabilities, which includes $2 million transferred from NCNG at the time of the sale of NCNG. PEC is unable to provide an estimate of the reasonably possible total remediation costs beyond what is currently accrued due to the fact that investigations have not been completed at all sites. This accrual has been recorded on an undiscounted basis. PEC measures its liability for these sites based on available evidence including its experience in investigating and remediating environmentally impaired sites. The process often involves assessing and developing cost-sharing arrangements with other PRPs. PEC will accrue costs for the sites to the extent its liability is probable and the costs can be reasonably estimated. Because the extent of environmental impact, allocation among PRPs for all sites, remediation alternatives (which could involve either minimal or significant efforts), and concurrence of the regulatory authorities have not yet reached to the stage where a reasonable estimate of the remediation costs can be made, PEC cannot determine the total costs that may be incurred in connection with the remediation of all sites at this time. It is anticipated that sufficient information will become available for several sites during 2005 to allow a reasonable estimate of PEC's obligation for those sites to be made.

Air Quality

There has been and may be further proposed legislation requiring reductions in air emissions for NOx, SO2, carbon dioxide and mercury. Some of these proposals establish nationwide caps and emission rates over an extended period of time. This national multi-pollutant approach to air pollution control could involve significant capital costs which could be material to PEC's consolidated financial position or results of operations. Control equipment that will be installed on North Carolina fossil generating facilities as part of the North Carolina legislation discussed below may address some of the issues outlined above. However, PEC cannot predict the outcome of this matter.

The EPA is conducting an enforcement initiative related to a number of coal-fired utility power plants in an effort to determine whether modifications at those facilities were subject to New Source Review requirements or New Source Performance Standards under the Clean Air Act. PEC was asked to provide information to the EPA as part of this initiative and cooperated in providing the requested information. The EPA initiated civil enforcement actions against other unaffiliated utilities as part of this initiative. Some of these actions resulted in settlement agreements calling for expenditures by these unaffiliated utilities, ranging from $1.0 billion to $1.4 billion. A utility that was not subject to a civil enforcement action settled its New Source Review issues with the EPA for $300 million. These settlement agreements have generally called for expenditures to be made over extended time periods, and some of the companies may seek recovery of the related cost through rate adjustments or similar mechanisms. PEC cannot predict the outcome of this matter.

In 2003, the EPA published a final rule addressing routine equipment replacement under the New Source Review program. The rule defines routine equipment replacement and the types of activities that are not subject to New Source Review requirements or New Source Performance Standards under the Clean Air Act. The rule was challenged in the Federal Appeals Court and its implementation stayed. In July 2004, the EPA announced it will reconsider certain issues arising from the final routine equipment replacement rule. Reconsideration does not impact the court-approved stay. The agency plans to issue a final decision on these reconsidered issues by year end. PEC cannot predict the outcome of this matter.

In 1998, the EPA published a final rule at Section 110 of the Clean Air Act addressing the regional transport of ozone (NOx SIP Call). Total capital expenditures to meet these measures in North and South Carolina could reach approximately $370 million, which has not been adjusted for inflation. PEC has spent approximately $284 million to date related to these expenditures. Increased operation and maintenance costs relating to the NOx SIP Call are not expected to be material to PEC's results of operations. Further controls are anticipated as electricity demand increases.

In 1997, the EPA issued final regulations establishing a new 8-hour ozone standard. In 1999, the District of Columbia Circuit Court of Appeals ruled against the EPA with regard to the federal 8-hour ozone standard. The U.S. Supreme Court has upheld, in part, the District of Columbia Circuit Court of Appeals decision. In April 2004, the EPA identified areas that do not meet the standard. The states with identified areas, including North and South Carolina are proceeding with the implementation of the federal 8-hour ozone standard. Both states promulgated final regulations, which will require PEC to install NOx controls under the states' 8-hour standard. The costs of those controls are included in the $370 million cost estimate above. However, further technical analysis and rulemaking may result in a requirement for additional controls at some units. PEC cannot predict the outcome of this matter.

In June 2002, legislation was enacted in North Carolina requiring the state's electric utilities to reduce the emissions of NOx and SO2 from coal-fired power plants. PEC expects its capital costs to meet these emission targets will be over $800 million by 2013. PEC has expended approximately $69 million of these capital costs through September 30, 2004. PEC currently has approximately 5,100 MW of coal-fired generation capacity in North Carolina that is affected by this legislation. The law requires the emissions reductions to be completed in phases by 2013, and applies to each utility's total system rather than setting requirements for individual power plants. The law also freezes the utilities' base rates for five years unless there are extraordinary events beyond the control of the utilities or unless the utilities persistently earn a return substantially in excess of the rate of return established and found reasonable by the NCUC in the utilities' last general rate case. Further, the law allows the utilities to recover from their retail customers the projected capital costs during the first seven years of the ten-year compliance period beginning on January 1, 2003. The utilities must recover at least 70% of their projected capital costs during the five-year rate freeze period. PEC recognized amortization of $20 million in the quarter ended September 30, 2004. No amortization was recognized in the quarter ended September 30, 2003. PEC recognized amortization of $50 million and $54 million in the nine months ended September 30, 2004 and 2003, respectively, and has recognized $124 million in cumulative amortization through September 30, 2004. Pursuant to the law, PEC entered into an agreement with the state of North Carolina to transfer to the state certain NOx and SO2 emissions allowances that result from compliance with the collective NOx and SO2 emissions limitations set out in the law. The law also requires the state to undertake a study of mercury and carbon dioxide emissions in North Carolina. Operation and maintenance costs will increase due to the additional personnel, materials and general maintenance associated with the equipment. Operation and maintenance expenses are recoverable through base rates, rather than as part of this program. PEC cannot predict the future regulatory interpretation, implementation or impact of this law.

In 1997, the EPA's Mercury Study Report and Utility Report to Congress conveyed that mercury is not a risk to the average American and expressed uncertainty about whether reductions in mercury emissions from coal-fired power plants would reduce human exposure. Nevertheless, the EPA determined in 2000 that regulation of mercury emissions from coal-fired power plants was appropriate. In 2003, the EPA proposed alternative control plans that would limit mercury emissions from coal-fired power plants. The first, a Maximum Achievable Control Technology (MACT) standard applicable to every coal-fired plant, would require compliance in 2008. The second, which the EPA has stated it prefers, is a mercury cap and trade program that would require limits to be met in two phases, 2010 and 2018. The EPA expects to finalize the mercury rule in March 2005. Achieving compliance with the proposal could involve significant capital costs which could be material to PEC's consolidated financial position or results of operations. PEC cannot predict the outcome of this matter.

In conjunction with the proposed mercury rule, the EPA proposed a MACT standard to regulate nickel emissions from residual oil-fired units. The agency estimates the proposal will reduce national nickel emissions to approximately 103 tons. The EPA expects to finalize the nickel rule in March 2005. PEC's oil-fired units have pollution controls in place, which would meet the proposed requirements of the nickel rule.

In December 2003, the EPA released its proposed Interstate Air Quality Rule, currently referred to as the Clean Air Interstate Rule (CAIR). The EPA's proposal requires 28 jurisdictions, including North Carolina, South Carolina, Georgia and Florida, to further reduce NOx and SO2 emissions in order to attain preset state NOx and SO2 emissions levels. The rule is expected to become final by the end of 2004. The air quality controls already installed for compliance with the NOx SIP Call and currently planned by PEC for compliance with the North Carolina law will reduce the costs required to meet the CAIR requirements for PEC's North Carolina units. Additional compliance costs will be determined once the rule is finalized.

In March 2004, the North Carolina Attorney General filed a petition with the EPA under Section 126 of the Clean Air Act, asking the federal government to force coal-fired power plants in thirteen other states, including South Carolina, to reduce their NOx and SO2 emissions. The state of North Carolina contends these out-of-state polluters are interfering with North Carolina's ability to meet national air quality standards for ozone and particulate matter. The EPA has not made a determination on the Section 126 petition, and PEC cannot predict the outcome of this matter.

Water Quality

As a result of the operation of certain control equipment needed to address the air quality issues outlined above, new wastewater streams may be generated at the applicable facilities. Integration of these new wastewater streams into the existing wastewater treatment processes may result in permitting, construction and requirements imposed on PEC in the immediate and extended future.

After many years of litigation and settlement negotiations the EPA adopted regulations in February 2004 for the implementation of Section 316(b) of the Clean Water Act. These regulations became effective September 7, 2004. The purpose of these regulations is to minimize adverse environmental impacts caused by cooling water intake structures and intake systems. Over the next several years these regulations will impact the larger base load generation facilities and may require the facilities to mitigate the effects to aquatic organisms by constructing intake modifications or undertaking other restorative activities. Substantial costs could be incurred by the facilities in order to comply with the new regulation. PEC currently estimates that from 2005 through 2009 the range of its expenditures to meet the Section 316(b) requirements of the Clean Water Act will be $20 million to $30 million.

Other Environmental Matters

The Kyoto Protocol was adopted in 1997 by the United Nations to address global climate change by reducing emissions of carbon dioxide and other greenhouse gases. Russia recently announced its intent to ratify the Protocol, which would allow the treaty to enter into force. The United States has not adopted the Kyoto Protocol, and the Bush administration has stated it favors voluntary programs. A number of carbon dioxide emissions control proposals have been advanced in Congress and by the Bush administration. Reductions in carbon dioxide emissions to the levels specified by the Kyoto Protocol and some legislative proposals could be materially adverse to PEC's consolidated financial position or results of operations if associated costs cannot be recovered from customers. PEC favors the voluntary program approach recommended by the administration and is evaluating options for the reduction, avoidance, and sequestration of greenhouse gases. However, PEC cannot predict the outcome of this matter.

Other Contingencies

1. As required under the Nuclear Waste Policy Act of 1982, PEC entered into a contract with the DOE under which the DOE agreed to begin taking spent nuclear fuel by no later than January 31, 1998. All similarly situated utilities were required to sign the same standard contract.

In 1995, the DOE issued a final interpretation that it did not have an unconditional obligation to take spent nuclear fuel by January 31, 1998. In Indiana Michigan Power v. DOE, the Court of Appeals vacated the DOE's final interpretation and ruled that the DOE had an unconditional obligation to begin taking spent nuclear fuel. The Court did not specify a remedy because the DOE was not yet in default.

After the DOE failed to comply with the decision in Indiana Michigan Power v. DOE, a group of utilities petitioned the Court of Appeals in Northern States Power (NSP) v. DOE, seeking an order requiring the DOE to begin taking spent nuclear fuel by January 31, 1998. The DOE took the position that its delay was unavoidable, and the DOE was excused from performance under the terms and conditions of the contract. The Court of Appeals found that the delay was not unavoidable, but did not order the DOE to begin taking spent nuclear fuel, stating that the utilities had a potentially adequate remedy by filing a claim for damages under the contract.

After the DOE failed to begin taking spent nuclear fuel by January 31, 1998, a group of utilities filed a motion with the Court of Appeals to enforce the mandate in NSP v. DOE. Specifically, this group of utilities asked the Court to permit the utilities to escrow their waste fee payments, to order the DOE not to use the waste fund to pay damages to the utilities, and to order the DOE to establish a schedule for disposal of spent nuclear fuel. The Court denied this motion based primarily on the grounds that a review of the matter was premature, and that some of the requested remedies fell outside of the mandate in NSP v. DOE.

Subsequently, a number of utilities each filed an action for damages in the Federal Court of Claims. The U.S. Circuit Court of Appeals (Federal Circuit) ruled that utilities may sue the DOE for damages in the Federal Court of Claims instead of having to file an administrative claim with DOE.

In January 2004, PEC filed a complaint with the DOE claiming that the DOE breached the Standard Contract for Disposal of Spent Nuclear Fuel by failing to accept spent nuclear fuel from various Progress Energy facilities on or before January 31, 1998. Damages due to DOE's breach will likely exceed $100 million. Similar suits have been initiated by over two dozen other utilities.

In July 2002, Congress passed an override resolution to Nevada's veto of DOE's proposal to locate a permanent underground nuclear waste storage facility at Yucca Mountain, Nevada. DOE plans to submit a license application for the Yucca Mountain facility by the end of 2004. In November 2003, Congressional negotiators approved $580 million for fiscal year 2004 for the Yucca Mountain project, $123 million more than the previous year. In January 2003, the State of Nevada, Clark County, Nevada, and the City of Las Vegas petitioned the U.S. Court of Appeals for the District of Columbia Circuit for review of the Congressional override resolution. On July 9, 2004, the Court rejected the challenge to the constitutionality of the resolution approving Yucca Mountain, but ruled that the EPA was wrong to set a 10,000-year compliance period. The DOE continues to state it plans to begin operation of the repository at Yucca Mountain in 2010. PEC cannot predict the outcome of this matter.

With certain modifications and additional approval by the NRC including the installation of onsite dry storage facilities at Robinson (2005) and Brunswick (2010), PEC's spent nuclear fuel storage facilities will be sufficient to provide storage space for spent fuel generated on its system through the expiration of the operating licenses for all of its nuclear generating units.

2. In 2001, PEC entered into a contract to purchase coal from Dynegy Marketing and Trade (DMT). After DMT experienced financial difficulties, including credit ratings downgrades by certain credit reporting agencies, PEC requested credit enhancements in accordance with the terms of the coal purchase agreement in July 2002. When DMT did not offer credit enhancements, as required by a provision in the contract, PEC terminated the contract in July 2002.

PEC initiated a lawsuit seeking a declaratory judgment that the termination was lawful. DMT counterclaimed, stating the termination was a breach of contract and an unfair and deceptive trade practice. On March 23, 2004, the United States District Court for the Eastern District of North Carolina ruled that PEC was liable for breach of contract, but ruled against DMT on its unfair and deceptive trade practices claim. On April 6, 2004, the Court entered a judgment against PEC in the amount of approximately $10 million. The Court did not rule on DMT's request under the contract for pending legal costs.

On May 4, 2004, PEC authorized its outside counsel to file a notice of appeal of the April 6, 2004, judgment and on May 7, 2004, the notice of appeal was filed with the United States Court of Appeals for the Fourth Circuit. On June 8, 2004, DMT filed a motion to dismiss the appeal on the ground that PEC's notice of appeal should have been filed on or before May 6, 2004. On June 16, 2004, PEC filed a motion with the trial court requesting an extension of the deadline for the filing of the notice of appeal. By order dated September 10, 2004, the trial court denied the extension request. On September 15, 2004, PEC filed a notice of appeal of the September 10, 2004 order and by order dated September 29, 2004, the appellate court consolidated the first and second appeals. DMT's motion to dismiss the first appeal remains pending.

PEC recorded a liability for the judgment of approximately $10 million and a regulatory asset for the probable recovery through its fuel adjustment clause in the first quarter of 2004. The Company cannot predict the outcome of this matter.

3. On February 1, 2002, filed a complaint with the Surface Transportation Board (STB) challenging the rates charged by Norfolk Southern Railway Company (Norfolk Southern) for coal transportation to certain generating plants. In a decision dated December 2003, the STB found that the rates were unreasonable and awarded reparations of $23 million and prescribed a methodology to determine maximum rates. Both parties petitioned for reconsideration of the December 2003 decision. On October 20, 2004, the STB reversed its December 2003 decision and concluded that the rates charged by Norfolk Southern were not unreasonable. The Company is in the process of evaluating future actions, which may include an application to the STB to phase in the new rates, or a judicial appeal. As of September 30, 2004, PEC has accrued a liability of $39 million, to return the reparations of $23 million, which was originally recorded as a regulatory liability, and accrue additional 2004 expenses of $16 million, of which $14 million, has been allocated to retail customers and recorded as deferred fuel cost while the remaining $2 million attributable to wholesale customers has been charged to fuel used in electric generation.

4. PEC and its subsidiaries are involved in various litigation matters in the ordinary course of business, some of which involve substantial amounts. Where appropriate, accruals have been made in accordance with SFAS No. 5, "Accounting for Contingencies," to provide for such matters. In the opinion of management, the final disposition of pending litigation would not have a material adverse effect on PEC's consolidated results of operations or financial position.

Exhibit D

CAROLINA POWER & LIGHT COMPANY
d/b/a PROGRESS ENERGY CAROLINAS, INC.

Historical Financial Statements

Consolidated Balance Sheet as of September 30, 2004

Consolidated Statements of Income for the Nine Months Ended September 30, 2004

Pro Forma Financial Statements

Unaudited Condensed Consolidation Pro Forma Balance Sheet as of September 30, 2004

Unaudited Condensed Consolidation Pro Forma Statements of Income for the Nine Months Ended September 30, 2004

Unaudited Pro Forma Capital Structure as of September 30, 2004

Progress Energy Service Company, LLC
P.O. Box 1551
Raleigh, NC 27602

CAROLINA POWER & LIGHT COMPANY
d/b/a PROGRESS ENERGY CAROLINAS, INC.

CONSOLIDATED BALANCE SHEET

As of September 30, 2004

Incorporated by reference is the Consolidated Interim Balance Sheet dated as of September 30, 2004 and the related Notes to Consolidated Interim Financial Statements per the attached Consolidated Interim Statements dated September 30, 2004.

Progress Energy Service Company, LLC
P.O. Box 1551
Raleigh, NC 27602

CAROLINA POWER & LIGHT COMPANY
d/b/a PROGRESS ENERGY CAROLINAS, INC.

CONSOLIDATED STATEMENTS OF INCOME

For the Nine Months Ended September 30, 2004

Incorporated by reference is the Consolidated Interim Statements of Income for the nine months ended September 30, 2004 and related Notes to Consolidated Interim Financial Statements per the attached Consolidated Interim Statements dated September 30, 2004.

Progress Energy Service Company, LLC
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CAROLINA POWER & LIGHT COMPANY d/b/a PROGRESS ENERGY CAROLINAS, INC.

UNAUDITED CONDENSED CONSOIDATED PRO FORMA FINANCIAL STATEMENTS

The following unaudited pro forma financial statements of the Company are based on the historical financial statements of the Company appearing elsewhere in this application. These pro forma financial statements have been prepared to reflect the proposed approvals requested in these applications to authorize the Company to enter up to a $500,000,000 5-1/4-year revolving credit agreement (the "Facility"). This Facility will be used by the Company in order to consolidate the Company's existing credit facilities, and to meet the Company's increased short-term capital needs arising in connection with the provision of electricity and related services to the Company's customers. The Company will not receive any proceeds from executing the Facility transactions. The Unaudited Condensed Consolidated Pro Forma Balance Sheet has been prepared assuming that the Facility had been executed on September 30, 2004. The Unaudited Condensed Consolidated Pro Forma Statements of Income for the nine months ended September 30, 2004 have been prepared as if the Facility had been executed at the beginning of the respective periods. The following unaudited pro forma financial data is presented for informational purposes only and is not necessarily indicative of the results of future operations.

Progress Energy Service Company, LLC
P.O. Box 1551
Raleigh, NC 27602

CAROLINA POWER & LIGHT COMPANY d/b/a PROGRESS ENERGY CAROLINAS, INC.

UNAUDITED CONDENSED CONSOLIDATED PRO FORMA BALANCE SHEET

As of September 30, 2004

(In thousands)

	Historical	Pro Forma Adjustments (A)	Pro Forma
ASSETS			
Electric Utility Plant, net	$ 8,535,136	$ -	$ 8,535,136
Cash and Cash Equivalents	18,418	-	18,418
Other Current Assets	1,060,077	-	1,060,077
Other Assets	1,352,600	-	1,352,600
Total Assets	$ 10,966,231	$ -	$ 10,966,231
LIABILITIES			
Common Stock, net	1,897,117	-	1,897,117
Retained Earnings	1,329,321	-	1,329,321
Preferred Stock	59,334	-	59,334
Long-term Debt, net	2,749,328	-	2,749,328
Current Portion of Long-term Debt	300,000	-	300,000
Other Current Liabilities	791,552	-	791,552
Accumulated Deferred Income Taxes	1,244,796	-	1,244,796
Other Liabilities and Deferred Credits	2,594,783	-	2,594,783
Total Liabilities and Equity	$ 10,966,231	$ -	$ 10,966,231

See Notes to Unaudited Condensed Consolidated Pro Forma Financial Statements.

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CAROLINA POWER & LIGHT COMPANY
d/b/a PROGRESS ENERGY CAROLINAS, INC.

UNAUDITED CONDENSED CONSOLIDATED PRO FORMA STATEMENT OF INCOME

For the Nine Months Ended September 30, 2004

	Historical	Pro Forma Adjustments	Pro Forma
Operating Revenues	$ 2,776,535	$ -	$ 2,776,535
Operating Expenses			
Fuel	636,803	-	636,803
Purchased Power	237,590	-	237,590
Other Operation and Maintenance	631,566	-	631,566
Depreciation and Amortization	393,110	-	393,110
Taxes Other than on Income	132,813	-	132,813
Income Tax Expense	215,817	6 (B)	215,823
Diversified Business	508	-	508
Total Operating Expenses	2,248,207	6	2,248,213
Operating Income	528,328	6	528,322
Other Income	688	-	688
Income Before Interest Charges	529,016	6	529,010
Interest Charges		467 (C)	
	143,043	(482) (D)	143,028
Net Income	385,973		385,982
Preferred Stock Requirements	(2,223)	-	(2,223)
Earnings for Common Stock	$ 383,750	$9	$ 383,759

See Notes to Unaudited Condensed Consolidated Pro Forma Financial Statements.

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CAROLINA POWER & LIGHT COMPANY
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NOTES TO UNAUDITED CONDENSED CONSOLIDATED PRO FORMA FINANCIAL STATEMENTS

(A) No proceeds will be received in the transaction; therefore the Company does not anticipate any change in the balance sheet.

(B) To adjust income taxes as a result of the net effect of the pro forma adjustments.

(C) To record the facility fees associated with the new Facility.

(D) To reverse the facility fees incurred on the existing revolving credit facilities that will be replaced with the new Facility.

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CAROLINA POWER & LIGHT COMPANY
d/b/a PROGRESS ENERGY CAROLINAS, INC.

UNAUDITED PRO FORMA CAPITAL STRUCTURE

As of September 30, 2004
(In thousands)

	Historical		Pro Forma	
Common Stock Equity	$ 3,226,438	53.4%	$ 3,226,438	53.4%
Preferred Stock	59,334	1.0%	59,334	1.0%
Long-term Debt, Net	2,749,328	45.6%	2,749,328	45.6%
Total Capitalization	$6,035,100		$6,035,100	

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